UPDATE

ON QUÉBEC'S ECONOMIC AND FINANCIAL SITUATION

Spring 2013

Finances et Économie
Québec

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Spring 2013

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Highlights

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The Québec Economy:
Recent Developments and Outlook for 2013 and 2014

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The Government's Financial Situation

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The Québec government's debt

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Implementation of the Economic Vision

HIGHLIGHTS

Today, the government is releasing the March 2013 update on Québec's economic and financial situation. It makes adjustments to the financial framework in Budget 2013-2014 of last November 20, reflecting the latest information on the economic situation and on the government's revenue and expenditure. This update confirms that:

— for 2012-2013, the budget deficit objective of $1.5 billion is maintained, as stipulated last November, as is the return to a balanced budget in 2013-2014.

Québec's economic and financial situation has changed since Budget 2013-2014 was tabled. The economy has continued to grow, despite the fragile global economic situation, though at a more moderate pace than forecast in late 2012. Uncertainty regarding the economic and budgetary situation in the euro area and the results of U.S. budget negotiations is contributing to more moderate economic growth than anticipated, resulting in a slight downward adjustment to the economic outlook for 2013 and 2014.

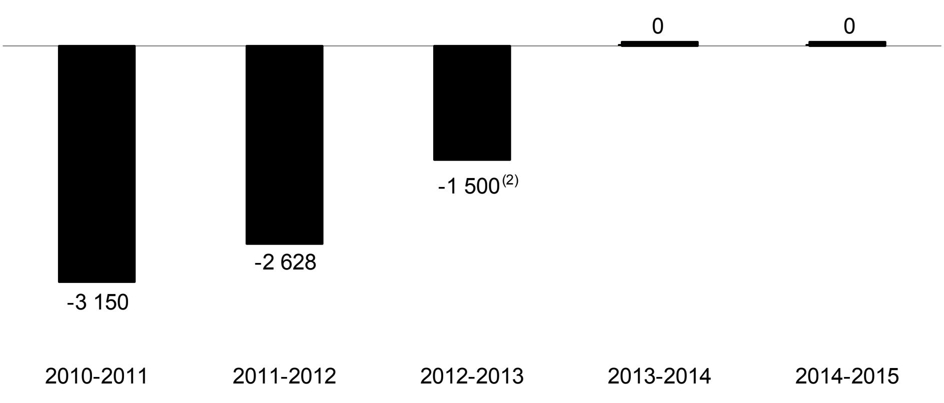
Concerning the budgetary situation:

— weak economic growth in the fourth quarter of 2012, in the United States, Canada and Québec, has resulted in less tax revenue than expected;

— these adjustments are offset in particular by a downward revision to debt service, additional equalization revenue and use of part of the contingency reserves.

CHART 1

Budgetary balance from 2010-2011 to 2014-2015(1)
(millions of dollars)



(1) Budgetary balance within the meaning of the *Balanced Budget Act*.
(2) For 2012-2013, the budgetary balance excludes the accounting impact arising from Hydro-Québec's exceptional loss from the closure of the Gentilly-2 nuclear power plant. The impact amounts to $1 876 million, i.e. $71 million more than the $1 805 million estimated at the time of Budget 2013-2014.

❑ Economic growth continues at a moderate pace

Since the budget was tabled on November 20, 2012, Québec has faced a difficult global economic situation. Uncertainty relating to the sovereign debt crisis in the euro area, bargaining over budgetary policy in the United States and slowing growth in emerging economies have all weighed on global economic activity.

Nonetheless, Québec's economy continued to grow at a moderate pace. While the economy's performance has been largely consistent with last November's forecasts, adjustments have been made to reflect weak economic growth in Québec, Canada and the United States, especially late in the year.

— Following real GDP growth of 1.0% in 2012, economic growth in Québec should amount to 1.3% in 2013 and 1.8% in 2014. This is a downward adjustment of 0.2 percentage point for these two years compared to the budget forecast last November.

The outlook for economic growth in Canada and the United States has also been revised since the budget.

— In Canada, real GDP should gain 1.7% in 2013 and 2.2% in 2014, a downward adjustment of 0.2 percentage point for 2013 and of 0.1 percentage point for 2014.

— In the United States, growth should amount to 1.8% in 2013, a negative adjustment of 0.2 percentage point, and then accelerate to 2.5% in 2014.

TABLE 1

Economic growth
(real GDP, percentage change)

	2012	2013	2014
Québec	1.0	1.3	1.8
Difference compared to Budget 2013-2014	*0.1*	*–0.2*	*–0.2*
Canada	1.8	1.7	2.2
Difference compared to Budget 2013-2014	*–0.1*	*–0.2*	*–0.1*
United States	2.2	1.8	2.5
Difference compared to Budget 2013-2014	*0.1*	*–0.2*	*0.0*

Sources: IHS Global Insight, Statistics Canada, Institut de la statistique du Québec, and Ministère des Finances et de l'Économie du Québec.

❑ Budgetary targets maintained

The government is maintaining the budgetary objectives set in Budget 2013-2014, despite more moderate economic growth.

The update to the financial framework reflects the recent change to the government's revenue and to the economic outlook for 2013 and 2014. Own-source revenue is adjusted downward by $250 million in 2012-2013 and $565 million in 2013-2014.

These adjustments stem in particular from:

- the lower yield from the QST resulting from weaker consumption than expected in the second half of 2012;
- lower revenue from corporate taxes attributable, in particular, to a less favourable international situation.

However, these adjustments are completely offset by:

- a reduction of the debt service because of lower interest rates than forecast;
- an unexpected increase in equalization payments further to updated economic and fiscal data;
- use of part of the contingency reserves incorporated in the November 2012 financial framework.

These changes make it possible to maintain the budgetary objectives set last November as they stand.

TABLE 2

Financial framework – Adjustments to Budget 2013-2014
(millions of dollars)

	2012-2013	2013-2014	2014-2015
BUDGETARY BALANCE – NOVEMBER 2012(1)	**–1 500**	—	—
Adjustments relating to the economic outlook			
Own-source revenue(2)	–250	–565	–575
Federal transfers	5	280	175
Debt service	95	85	200
	–150	**–200**	**–200**
Other adjustments			
Sommet sur l'enseignement supérieur			
Reduction of the rate of the tax credit for tuition fees and examination fees from 20% to 8%	—	34	61
Additional spending relating to the improvement to the student financial assistance program(3)	—	–34	–61
Use of the contingency reserves	150	200	200
	150	**200**	**200**
Total adjustments	**—**	**—**	**—**
BUDGETARY BALANCE – MARCH 2013(1)	**–1 500**	**—**	**—**
As a % of GDP	***–0.4***	**—**	**—**

(1) Budgetary balance within the meaning of the *Balanced Budget Act*.
(2) Excludes savings arising from the adjustment to student financial assistance.
(3) For details on the improvement to student financial assistance, see section D, "Implementation of the Economic Vision".

Moreover, the financial framework reflects the decisions made following the Sommet sur l'enseignement supérieur, held last February 25 and 26, concerning student financial assistance in particular.

— The improvements to student financial assistance result in a $34-million increase in program spending in 2013-2014 and a $61-million increase in 2014-2015, in particular for the gradual rise to $45 000 of the parents' income threshold beyond which their income is considered in the calculation of student assistance. These measures will be funded by reducing the rate of the tax credit for tuition fees and examination fees from 20% to 8%.

❑ Disciplined spending management

The government's commitment to meet the objectives for restoring fiscal balance is tied to maintaining the spending objectives set in the last budget.

— Apart from the additional spending relating to the improvement to the student financial assistance program, which is funded by an equivalent reduction in the tax credit for tuition and examination fees, no other adjustment is planned for program spending.

For 2012-2013, the program spending growth objective remains unchanged at 1.9%. For the following two years, growth will be 1.9% and 2.5% respectively.

Such results are possible thanks to disciplined spending management and the participation of all government departments and organizations in this effort.

TABLE 3

Program spending – Adjustments to Budget 2013-2014
(millions of dollars)

	2012-2013	2013-2014	2014-2015
NOVEMBER 2012	**62 642**	**63 791**	**65 350**
% change	***1.9***	***1.8***	***2.4***
Additional spending relating to the improvement to the student financial assistance program(1)	—	34	61
MARCH 2013	**62 642**	**63 825**	**65 411**
% change	***1.9***	***1.9***	***2.5***

(1) For details on the improvement to student financial assistance, see section D, "Implementation of the Economic Vision".

❑ Debt reduction objectives

The government is again confirming that the debt reduction objectives written into the *Act to reduce the debt and establish the Generations Fund* are maintained:

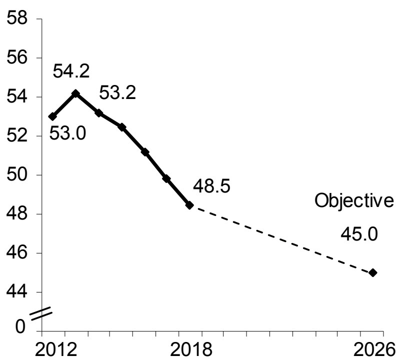
— 45% of GDP for the gross debt as at March 31, 2026;

— 17% of GDP for the debt representing accumulated deficits as at March 31, 2026.

CHART 2

Gross debt as at March 31

(as a percentage of GDP)

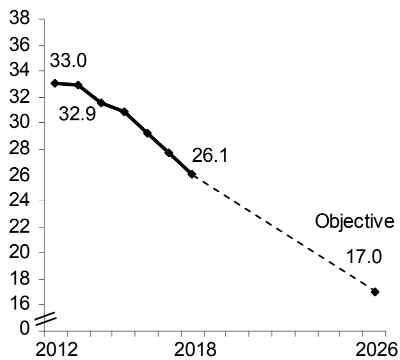


Note: The gross debt excludes borrowings made in advance and takes the amounts accumulated in the Generations Fund into account.

CHART 3

Debt representing accumulated deficits as at March 31

(as a percentage of GDP)



To achieve its debt reduction objectives, the government announced, in the November 20, 2012 budget, that it will deposit in the Generations Fund:

— the revenue resulting from indexing the price of heritage electricity as of 2014. This will amount to $95 million in 2014-2015, $190 million in 2015-2016, $290 million in 2016-2017 and $395 million in 2017-2018;

— all mining royalties as of 2015-2016. This will amount to $315 million in 2015-2016 and $360 million per year thereafter;

— the revenue, as of 2017-2018, stemming from the increase in Hydro-Québec's net profits resulting from the closure of the Gentilly-2 nuclear power plant. This will amount to $215 million per year;

— as of 2014-2015, $100 million per year arising from the increase in the specific tax on alcoholic beverages.

The government also announced a reduction in planned capital investments of $1.5 billion per year as of 2013-2014.

These debt reduction measures will allow the government to achieve the objectives set in the *Act to reduce the debt and establish the Generations Fund*.

❑ Implementation of the economic vision

In Budget 2013-2014, the government set out the vision that will guide how it acts on the economy. This vision is based on the certainty that investment is necessary to secure our prosperity.

In particular, the economic vision focuses on private investment as the key to future growth. Accordingly, several measures in favour of private investment were put in place immediately and others are in preparation.

The March 2013 economic and financial update provides the government with an opportunity to report on many of its commitments, including university funding.

It is also an opportunity to set out the government's action in favour of business, in particular with the creation of the Banque de développement économique du Québec, two new economic diversification funds and a framework for takeover bids of Québec companies.

The *Update on Québec's Economic and Financial Situation* also specifies sector-based actions for economic development.

Section A

THE QUÉBEC ECONOMY: RECENT DEVELOPMENTS AND OUTLOOK FOR 2013 AND 2014

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INTRODUCTION

This section updates the economic forecasts that underpin the government's financial framework.

❑ The Québec economy continues to grow, despite a difficult global context

The year 2012 was not an easy one on the economic front.

— Uncertainty stemming from the euro area sovereign debt crisis weighed on global economic activity and several leading economies in the euro area experienced a recession.

— Fiscal policy negotiations curtailed economic growth in the United States. The U.S. economy stagnated in the fourth quarter and the average unemployment rate exceeded 8% in 2012.

— Economic growth in Canada also slowed, to below 2%.

— Flagging demand in the advanced economies dampened growth in the emerging economies and caused the price of commodities to fall.

— Businesses thus operated in a context of gradually dwindling profits.

Consequently, growth continued in Québec at a moderate pace. Furthermore, growth in consumption was less than expected.

— The change in recent data indicates 1.0% growth in real gross domestic product (GDP) in 2012.

Furthermore, growth in employment continued in late 2012. Some 30 800 jobs were created last year, a 0.8% increase. The average unemployment rate stood at 7.8% in 2012.

❑ A strengthening of growth in 2013 and 2014

The economic growth should accelerate in Québec in 2013 and 2014, because of the gradual improvement of the world economy. Stronger growth is expected in United States, in particular from the second quarter of 2013.

— Real GDP growth in Québec should reach 1.3% in 2013 and 1.8% in 2014.

— This represents nevertheless a revision of 0.2 percentage point for each of these two years, compared to the November 2012 forecast, in order to take into account a slower dissipation of the global downturn.

1. THE ECONOMIC SITUATION IN QUÉBEC

Economic growth should accelerate in Québec in 2013 and 2014, in particular because of stronger growth in the United States expected as of the second half of 2013 and the gradual improvement in the global economy.

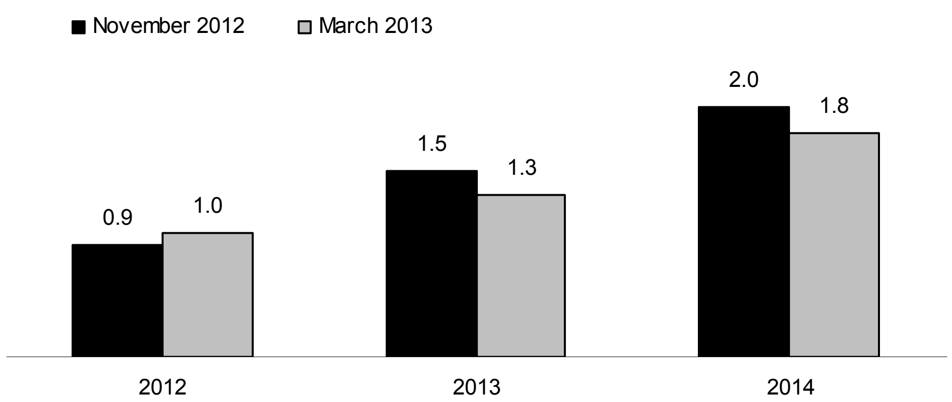
— Following a 1.0% growth in 2012, the economic outlook in the March 2013 Québec economic and financial update anticipates 1.3% growth in real GDP in 2013, and 1.8% in 2014.

The evolution of the economy conforms for the most part to the November 2012 forecasts, which anticipated 1.5% growth in real GDP in 2013, and 2.0% in 2014.

— This nonetheless means a 0.2 percentage point downward adjustment in real GDP in 2013 and in 2014 in relation to the November forecast, to take into account, in particular, the slower than anticipated dissipation of the global downturn.

CHART A.1

Economic growth in Québec
(real GDP, percentage change)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

1.1 Components of real GDP

The anticipated 1.3% and 1.8% growth in real GDP in 2013 and 2014, respectively, will be sustained by domestic demand and more robust exports.

- Given the sound performance of the labour market and the gradual dissipation of uncertainty stemming, in particular, from the global economic context, the situation will be more favourable to household consumption.
- Non-residential business investment should continue to grow in 2013 and 2014.
  - Business investment will continue to be sustained by a strong Canadian dollar, making imported equipment accessible, by low interest rates and by the sound financial health of businesses.
- Moreover, despite a difficult international context, exports continued to rise in 2012 and the gradual improvement in the global economic situation in 2013 and 2014 should further sustain international demand for Québec products.
- On the other hand, residential investment should decline in 2013 and 2014, especially as a result of new measures that the federal government has implemented to limit mortgage debt in Canada.
- Furthermore, the contribution made by all governments to economic growth will be limited, since they are pursuing deficit-reduction efforts.

TABLE A.1

Real GDP and its major components
(percentage change)

	2011	2012	2013	2014
Domestic demand				
Consumption	2.3	1.1	1.8	2.1
Residential investment	0.7	2.1	–4.6	–1.1
Non-residential business investment	6.6	7.6	2.0	3.7
Government expenditures and investments	1.8	1.1	0.3	0.6
External trade				
Total exports	–0.2	1.7	2.8	3.0
Total imports	4.2	1.3	2.3	2.4
Real GDP	**1.9**	**1.0**	**1.3**	**1.8**

Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

1.2 Labour market

The Québec labour market has been robust in recent years. Following the creation of 66 700 jobs in 2010 and 38 500 jobs in 2011, 30 800 jobs were created in 2012, a 0.8% increase over the preceding year. In 2012, the average unemployment rate stood at 7.8%, the same level as in 2011, but fell in the second half of the year.

— This labour market vitality reflects the resilience of the Québec economy, despite a difficult international context.

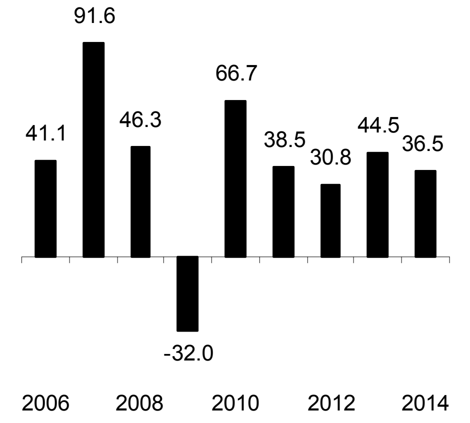
The anticipated improvement in economic growth should boost employment by 1.1% in 2013 and 0.9% in 2014, equivalent to 44 500 and 36 500 jobs, respectively.

Moreover, the upturn on the Québec labour market has led to a gradual reduction in the unemployment rate since 2009. With ongoing job creation, the unemployment rate should continue to fall, from 7.8% in 2012 to 7.5% in 2013 and 7.4% in 2014.

— Accordingly, the Québec labour market continues to improve gradually in relation to the other provinces in Canada.

CHART A.2

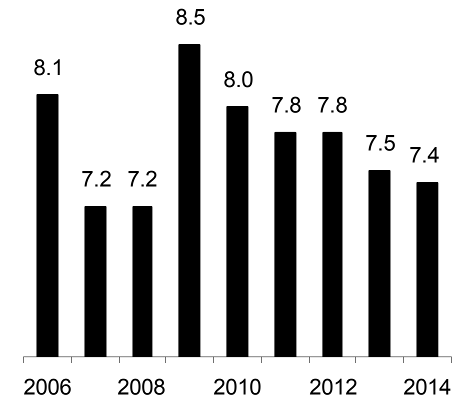
Job creation in Québec
(change in thousands)



Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.3

Unemployment rate in Québec
(per cent)



Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

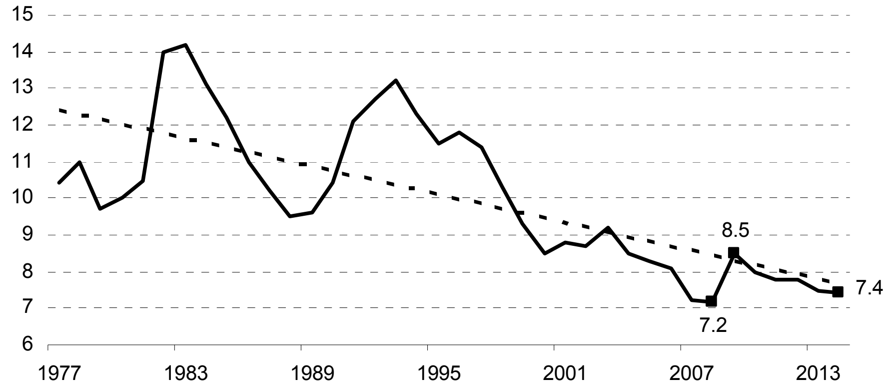
Long-term labour market trends

Stimulated by public policies, the labour market initiated significant adjustments to contend with demographic change. The gradual reduction in the unemployment rate occurred simultaneously with broader labour force participation. In particular, for the population in the 15 to 64 age group:

- the unemployment rate fell from 10.1% in 1980 to 7.8% in 2012;
- the participation rate rose from 67.7% in 1980 to 77.7% in 2012;
- the employment rate increased from 60.8% in 1980 to 71.6% in 2012.

Accordingly, differences on the labour market between Québec and the rest of Canada have virtually disappeared.

Unemployment rate in Québec – Population 15 years of age and over
(per cent)



Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

Key labour market indicators – Population 15 to 64 years of age
(per cent)

	Unemployment rate		Participation rate		Employment rate	
	Québec	Rest of Canada	Québec	Rest of Canada	Québec	Rest of Canada
1980	10.1	6.8	67.7	73.1	60.8	68.1
1990	10.5	7.5	72.9	78.0	65.3	72.1
2000	8.5	6.4	73.4	77.0	67.1	72.1
2010	8.0	8.1	77.3	78.0	71.1	71.7
2012	7.8	7.2	77.7	78.0	71.6	72.4

Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

1.3 Household spending

Growth in household spending should continue at a moderate pace.

— As forecast in November, household spending should accelerate and grow by 1.8% in 2013 and 2.1% in 2014.

In 2012, household spending, especially on goods, increased only modestly. Such spending suffered the after-effects of a second increase in the Québec sales tax (QST) on January 1, 2012, in addition to the impact of fragile consumer confidence.

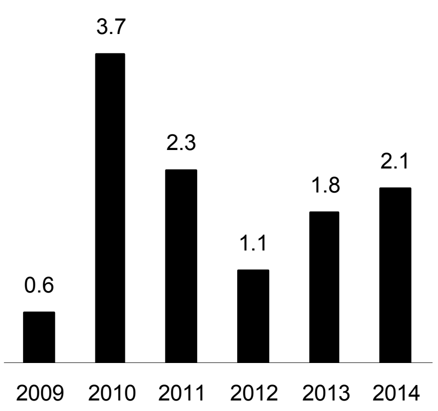
The anticipated upswing in household spending stems, in particular, from higher employment and wages and improving consumer confidence.

— Consumer confidence was highly volatile in 2012 and should gradually become more robust in the coming months with the growing attenuation of worldwide uncertainty.

On the other hand, the anticipated downturn in residential investment will alter the composition of consumption, limiting growth in goods purchases, such as construction materials, furniture and household appliances.

CHART A.4

Household consumption expenditures in Québec
(percentage change, in real terms)

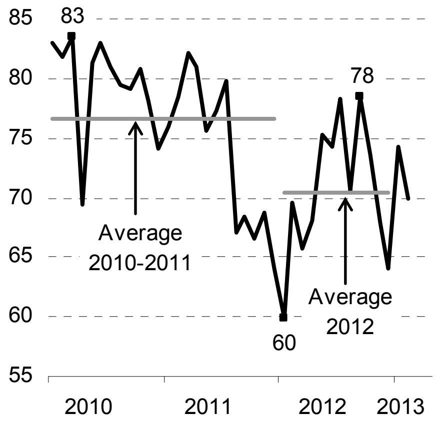


Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.5

Consumer confidence in Québec

(index, year 2002 = 100)



Sources: Conference Board of Canada and Ministère des Finances et de l'Économie du Québec.

1.4 Residential investment

Residential investment should decline by 4.6% in 2013 and 1.1% in 2014. This downward trend reflects, in particular, changes in housing starts, which will gradually reach levels in keeping with the household formation in Québec.

— Housing starts will thus fall by 12.6% in 2013, to 41 400 units, and by 3.3% in 2014, to 40 100 units.

The downturn in residential investment will stem, notably, from the impact of measures that the federal government introduced to curb the growth of mortgage credit in Canada.

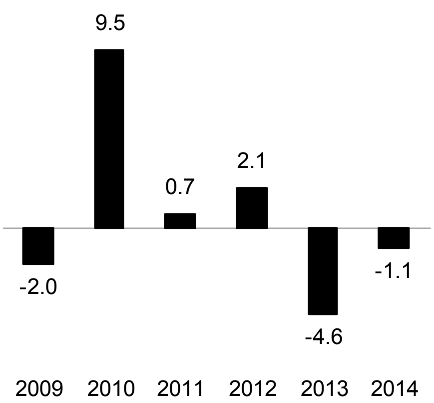
— However, current low interest rates and ongoing job creation will continue to support the residential sector in Québec, which should experience a soft landing.

— Despite the projected declines, housing starts will remain at higher levels, i.e. over 40 000 units per year, than those seen in the late 1990s, when they were below 30 000 units.

CHART A.6

Residential investment in Québec

(percentage change, in real terms)

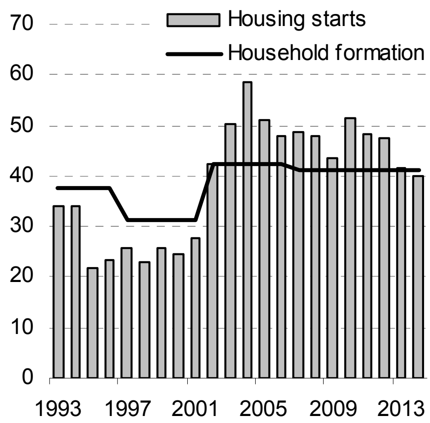


Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.7

Housing starts and household formation in Québec

(thousands of units)



Sources: Institut de la statistique du Québec, Statistics Canada, Canada Housing and Mortgage Corporation and Ministère des Finances et de l'Économie du Québec.

Weakening growth in the residential sector

The residential sector has been very dynamic since 2002

The Québec residential sector has experienced a strong activity since 2002.

- The number of housing starts rose from an average of 29 400 units per year between 1991 and 2001 to 48 800 units, on average, between 2002 and 2012.
- Between 2002 and 2012, the average price of existing housing units increased by 8.3% per year.

Certain indicators suggest that the upward cycle in the residential sector is winding down

Between 2002 and 2012, the number of housing starts outstripped household formation, which stood on average around 42 000 households per year, thereby resolving the shortage observed in the early 2000s, in particular in the rental housing sector.

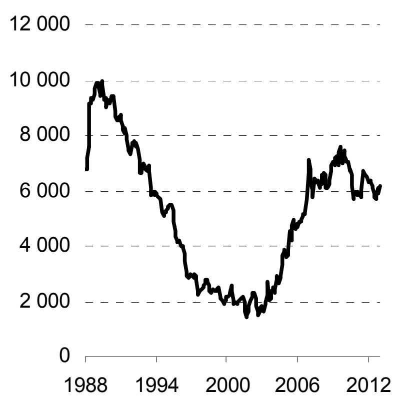
This situation led to some accumulation of unsold new housing stock, especially in multi-dwelling structures.

- However, this stock has not reached the peaks of the late 1980s and has stabilized at around 6 000 units in recent years.

Furthermore, from the standpoint of rental housing, the increase in housing starts has been beneficial.

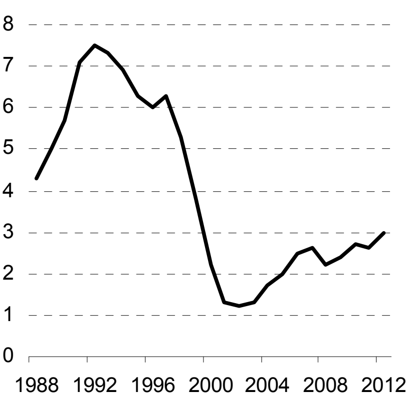
- Indeed, the rental market, which experienced shortages at the beginning of the decade with vacancy rates of roughly 1%, was restored to balance with a vacancy rate of 3.0% in 2012.

Unsold new housing stock[1]
(units)



(1) Population centres with 50 000 or more inhabitants.
Source: Canada Housing and Mortgage Corporation.

Vacancy rates of rental housing units
(per cent)



Source: Canada Housing and Mortgage Corporation.

Weakening growth in the residential sector (continued)

Currently low interest rates mean that property remains fairly affordable, although increases in property prices have outstripped increases in household income in recent years.

- Mortgage interest rates are destined to remain low and only rise gradually in the coming quarters. Furthermore, growth in household income will largely offset the interest rate increases anticipated in the coming years.
- However, should mortgage rates rise sharply, property could become less accessible.

Activity in the residential sector is flagging, but an abrupt correction is not anticipated

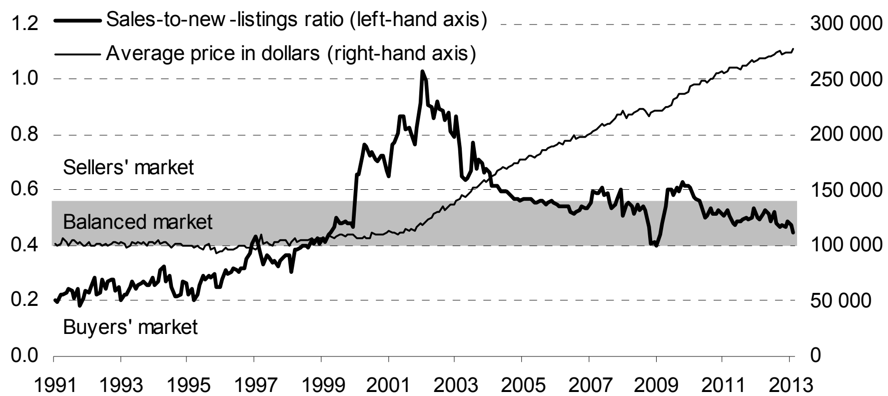
Since July 2012, activity in the residential sector has slowed markedly in Québec, in particular in reaction to the introduction by the federal government of new measures concerning insured mortgage loans, including the reduction in the maximum amortization period from 30 years to 25.

- After these measures took effect, housing starts fell by 4.7% and 11.0% in the third and fourth quarters of 2012, respectively, while sales of existing homes declined by 7.0% and 3.8%, respectively.

Despite the downturn observed in recent months, the home resale market remained balanced in February 2013, with a sales-to-new-listings ratio of 0.45.[1]

Accordingly, the relationship between supply and demand is neither to the advantage of sellers (excessive demand, upward pressure on prices) nor to that of buyers (insufficient demand, downward pressure on prices). In this context, the price of existing homes should continue to rise at a pace similar to inflation.

Conditions on the home resale market and average price in Québec
(ratio and average price in dollars)



Sources: Canadian Real Estate Association and Ministère des Finances et de l'Économie du Québec.

1 According to the Canada Mortgage and Housing Corporation, the home resale market is balanced when the sales-to-new-listings ratio ranges from 0.4 to 0.55.

1.5 Non-residential investment

Non-residential investment is a key driving force of economic activity in Québec. Since the last recession, Québec firms have taken over from governments as far as investment is concerned and have sustained economic growth.

The high level of non-residential investment, especially by businesses, should continue in the coming years.

— Following 3.1% growth in 2010, 6.1% in 2011 and 8.1% in 2012, growth in total non-residential investment should stand at 1.9% in 2013. In 2014, this growth should reach 3.0% and the investments should total 57.2 billions of dollars.

❑ Government investments

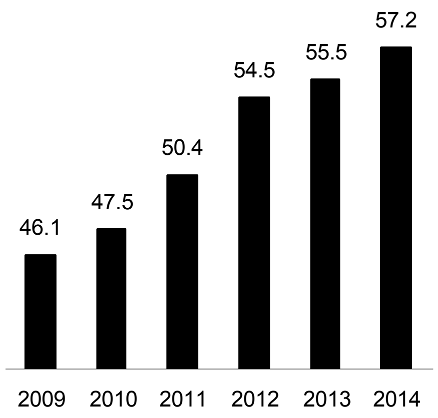
In November 2012, the Québec government committed itself to reconciling the need to develop and renew infrastructure with its financial capacity and to enhancing the management of investments, thereby acting upon the recommendations in the report prepared by SECOR-KPMG.

— Overall public investments in Québec should, accordingly, decline by 2.1% in 2013 and 1.9% in 2014.

— The level of such investment will nonetheless still be significant, standing close to 19 billions of dollars in the following years. Indeed, the forecast downturn is occurring after the outstanding growth that occurred during the recession, when government support sustained economic activity.

CHART A.8

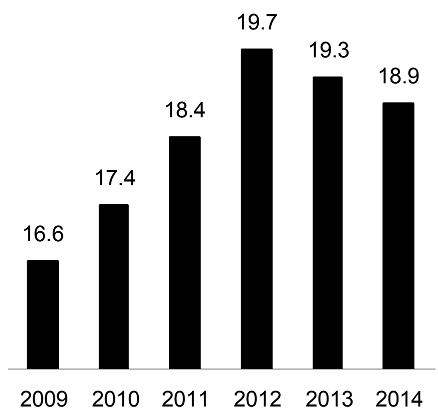
Total non-residential investment in Québec
(billions of dollars, in nominal terms)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.9

Government investments in Québec
(billions of dollars, in nominal terms)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

Invest to ensure Québec's prosperity

The Québec economy is open to a world that is undergoing sweeping changes. On foreign markets as on the domestic market, Québec firms must deal with keen competition.

- Investment plays a crucial role in enhancing business competitiveness, thereby ensuring job creation and an improvement in Quebecers' standard of living.

In order to foster private investment, the government introduced several initiatives in its Budget 2013-2014, in particular:[1]

- measures of a fiscal nature, notably the implementation of a new tax holiday for major investment projects involving at least $300 million, THI, and the extension and enhancement of the investment tax credit available in all regions;
- the implementation of new tools to support businesses wishing to invest in Québec, through the establishment of the Banque de développement économique du Québec;
- the establishment of economic diversification funds for the regions affected by the abandonment of the production of asbestos and nuclear energy to help them make the transition to promising niches, namely the Asbestos, Mauricie and Centre-du-Québec regions;
- the establishment of a $200-million fund to support the electrification of transportation and the development of clean technologies.

Investment initiatives must target all sectors producing goods and services, in particular those in which Québec enjoys comparative advantages, including innovative sectors and those related to natural resources.

- Québec must, accordingly, invest more extensively in **high added-value sectors**, where Québec firms have an advantage from the standpoint of technology and creativity.
- Québec must **rely on niches of excellence**, such as the development of the electrification of transportation and clean technologies that allow businesses to reduce their environmental impact.
- Québec **has significant mineral resources** for which worldwide demand has been rising for several years because of the development of emerging economies. Mining operations are a source of prosperity and job creation.
- On the **energy** front, it is in Québec's interests to pursue the development of its renewable resources. Moreover, Québec should also develop its oil potential, consistent with the most stringent environmental and social acceptance practices, to reduce its dependency and imports.

1 To obtain additional information on investment in Québec and the measures intended to foster private investment, please see the document entitled *Investing for Our Prosperity* published in conjunction with Budget 2013-2014.

❑ Business investment

Following a 6.5% upturn in 2011, growth in business investment remained robust, at 9.1% in 2012.

— Favourable borrowing conditions fostered such growth, through highly advantageous interest rates and the sound financial health of Québec firms.

Growth in business investment should continue and should reach 4.0% in 2013 and 5.6% in 2014.

— However, the climate of uncertainty that has affected the world economy over the past year could encourage companies to be cautious in 2013.

Nonetheless, Québec firms continue to benefit from conditions favourable to increasing their capital base and bolstering productivity.

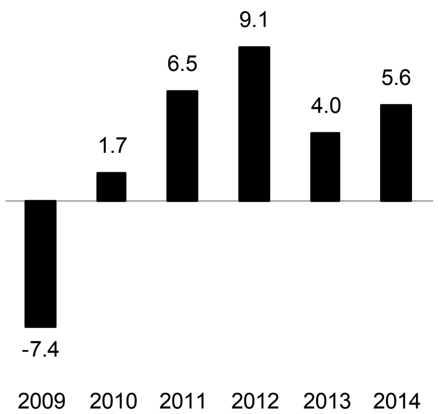
— The Canadian dollar, which remains high, is making accessible imported machinery and promoting investments in machinery and equipment.

— Investments in machinery and equipment should grow by 4.0% in 2013 and 5.7% in 2014.

CHART A.10

Business investment in Québec

(percentage change, in nominal terms)

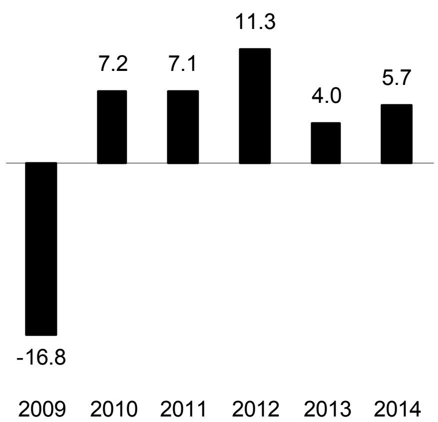


Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.11

Business investment in machinery and equipment in Québec

(percentage change, in nominal terms)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

1.6 Foreign trade

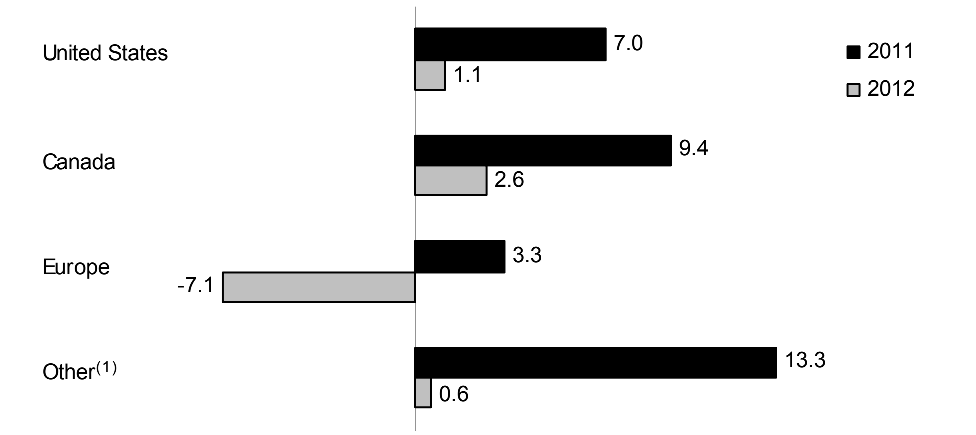
Québec is an open economy that is significantly influenced by the economic situation of its trading partners. Exports account for over 45% of Québec's GDP.

In 2012, several external factors curbed Québec's foreign trade, in particular the sovereign debt crisis in the euro area, moderate economic growth in Canada and the United States, and dampened growth in the emerging economies.

The influence of such factors should lessen as of 2013 with the gradual acceleration of global growth. Accordingly, Québec will benefit from the strengthening of the world economy, in particular that of the United States, which will bolster exports.

CHART A.12

Québec goods exports by destination
(percentage change, in nominal terms)



(1) Includes, in particular, China, Japan, Mexico, Brazil, India and Australia.
Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

❑ Exports

In 2012, global uncertainty stemming from budget negotiations in the United States, the recession in the euro area and the slowdown in emerging economies weighed on Québec exports.

— Despite this difficult context, total exports rose by 1.7% in 2012, in real terms.

— Exports should increase by 2.8% in 2013 and 3.0% in 2014. In the coming years, they will benefit from a more robust world economy, with the gradual reduction of difficulties in Europe and the acceleration of growth in the United States.

❑ Imports

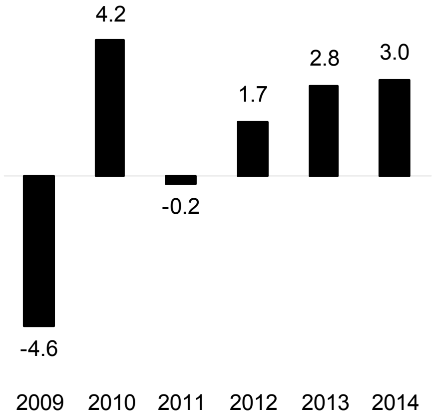
Québec mainly imports consumer goods, machinery and equipment and inputs for the manufacture of products.

— Imports climbed by 1.3% in 2012, a reflection of more modest growth in domestic demand.

— Growth in imports should stand at 2.3% in 2013 and 2.4% in 2014, in keeping with domestic demand and exports.

CHART A.13

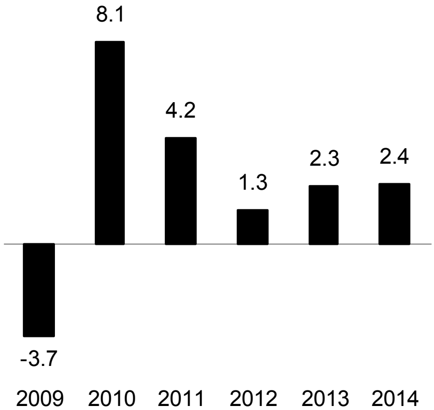
Québec's total exports
(percentage change, in real terms)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.14

Québec's total imports
(percentage change, in real terms)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

❑ Net exports

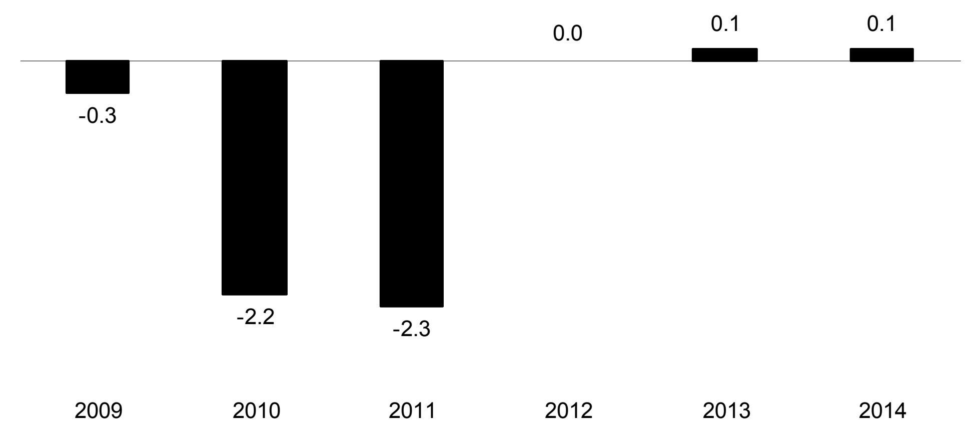
Exports, which will benefit from a more favourable global economic context, and the modest upturn in imports will mean that Québec's net exports will make a positive contribution to economic growth.

Accordingly, foreign trade should make a slightly positive contribution to economic activity in 2013 and 2014.

— However, this situation marks a noticeable improvement in relation to the situation observed in 2010 and 2011, when the external sector made a pronounced negative contribution to economic activity in Québec.

CHART A.15

Contribution of net exports to growth in Québec's real GDP
(percentage points)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

Outlook for U.S. demand for Québec products

U.S. demand for Québec products will continue to grow

Québec's international exports are closely tied to American demand for Québec products. According to this indicator, Québec exports should continue to benefit from the gradual upturn in the U.S. economy.

- After increasing by 7.0% in 2012, the index of U.S. demand for Québec products[1] should grow by 3.6% in 2013 and by 4.2% in 2014.

The revival of the U.S. manufacturing sector should continue to support exports of machinery, equipment and intermediate products, while demand for transportation products should continue.

- After several difficult years, the turnaround in the American real estate sector should foster exports of construction materials.

U.S. demand for Québec products is not fully restored

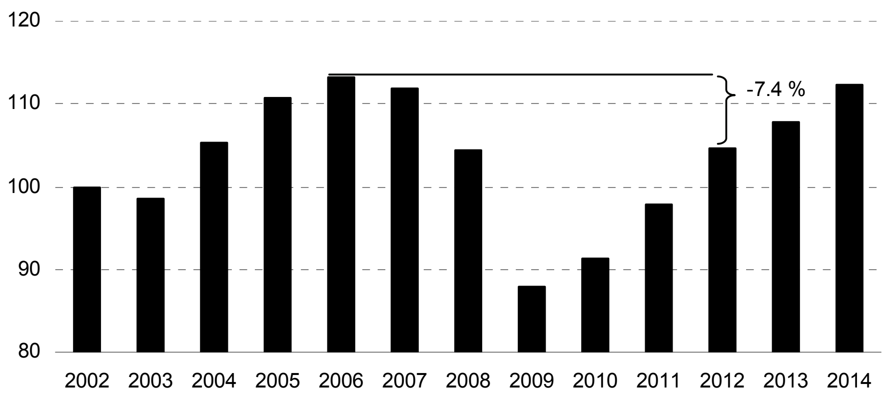
In 2012, the index of U.S. demand for Québec products was still 7.4% below its 2006 peak. This situation stems, particularly, from the still partial recovery of the American economy after the fall observed in the last recession.

- Employment in the United States remains 2.2% below its previous peak (–3 million jobs), industrial output is 2.1% lower, while real business investment is below 5.1% its level of six years ago.

American demand for Québec products will only regain pre-recession levels when the United States economy has recovered fully.

- Indeed, the index of U.S. demand for Québec products should take several more years to return to the level attained in 2006.

Index of U.S. demand for Québec products
(index, year 2002 = 100)



Sources: Institut de la statistique du Québec, IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

1 More complete information on the composition of the index is available on page 30 of the *Update on Québec's Economic and Financial Situation* published in the fall of 2009.

Change in the balance of trade and oil imports

Since 2003, the deficit in Québec's trade balance has grown. In 2011, it reached $28.7 billion, equivalent to 8.3% of GDP.

Several factors explain the deterioration in the balance of trade:

- the sustained appreciation in the Canadian dollar stimulated growth in imports and slowed that in exports. The Canadian dollar rose from an average of US$0.64 in 2002 to US$1.01 in 2011;
- exporters faced several difficulties, notably the bursting of the technology bubble, weak economic growth in the United States and growing competition from emerging economies.

Moreover, Québec is a net importer of oil. In 2011, international crude oil imports, worth $10.9 billion, accounted for nearly 40% of the trade deficit. In 2009, the value of crude oil imports was reduced considerably because of the fall in prices. In 2010 and 2011, the value of imports did not rise significantly, despite markedly higher prices, especially because of the closing of Shell's Montréal-Est refinery in October 2010.

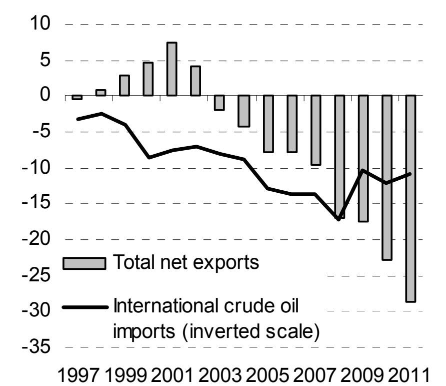
- The closing led to a reduction in crude oil imports but also to a drop in exports of refined products.

The Québec economy is becoming increasingly efficient in its use of oil. Oil consumption per unit of GDP fell by 35% between 1984 and 2009. Despite this improved efficiency, economic expansion and the enhancement of the standard of living are accompanied by increased energy consumption.

The consumption of energy produced from oil accounts for nearly 40% of total energy consumption in Québec. This share remained fairly constant between 1984 and 2009. While a number of measures have been implemented to reduce dependency on oil, this resource will remain an essential input in the economy for several years.

Balance of trade and international crude oil imports

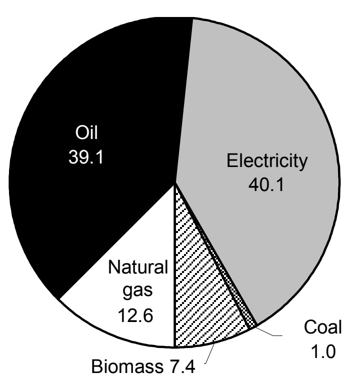
(billions of dollars, in nominal terms)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

Final energy consumption in Québec – 2009

(as a percentage of total energy consumption)



Sources: Statistics Canada and Ministère des Ressources naturelles du Québec.

1.7 Nominal GDP

Nominal GDP, which measures the value of output bearing in mind the impact of prices, should grow by 3.6% in 2013 and 3.9% in 2014.

— Growth in nominal GDP will be sustained by an increase in real GDP of 1.3% in 2013 and 1.8% in 2014, and by higher prices for the goods and services that Québec produces or imports of 2.2% in 2013 and 2.0% in 2014.

The increase in nominal GDP will be reflected in increases in the key tax bases of the government. In nominal terms:

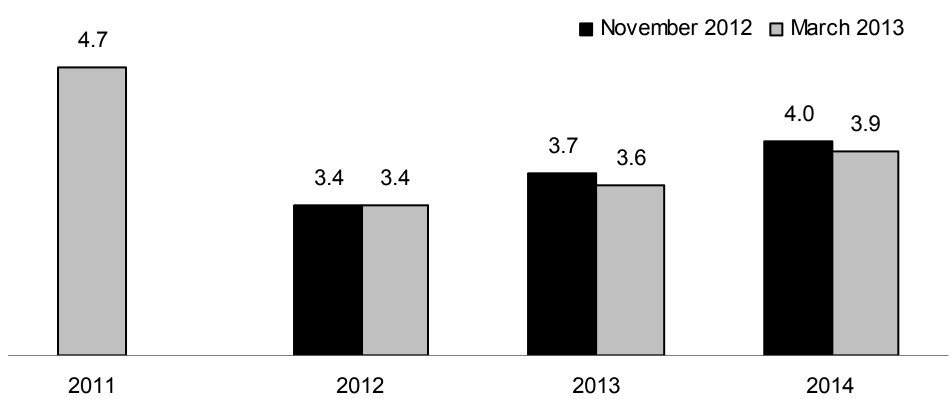
— the net operating surplus of corporations[1] will rise by 4.9% in 2013 and 7.0% in 2014;

— wages and salaries will increase by 3.5% in 2013 and 3.4% in 2014;

— consumption will rise by 3.4% in 2013 and 3.6% in 2014.

CHART A.16

Change in nominal GDP in Québec
(percentage change)



Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

1 According to the new nomenclature used by Statistics Canada, the net operating surplus of companies includes, in particular, the profits and investment income of enterprises.

❑ Consumer price index

The consumer price index (CPI) increased by 2.1% in 2012, spurred, in particular, by the rise in the Québec sales tax on January 1, 2012.

The CPI should climb by 1.6% in 2013 and 1.9% in 2014.

— The slower growth in the CPI is largely attributable to the end of the impact on prices stemming from higher consumption taxes.

TABLE A.2

Change in GDP and prices indexes
(percentage change)

	2011	2012	2013	2014
Real GDP	1.9	1.0	1.3	1.8
Nominal GDP	4.7	3.4	3.6	3.9
GDP price index – GDP deflator	2.7	2.3	2.2	2.0
Consumer price index	3.0	2.1	1.6	1.9

Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

1.8 Comparison with private sector forecasts

The economic growth forecast of the Ministère des Finances et de l'Économie du Québec for 2013 and 2014 falls slightly below the average of private sector forecasts.

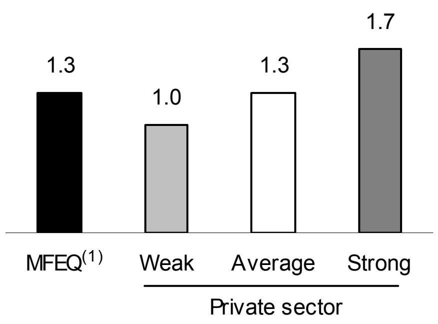
— In 2013, the forecast 1.3% growth in real GDP is identical to the average private sector forecast.

— In 2014, the forecast 1.8% growth in real GDP is below the 2.1% average private sector forecast.

The magnitude of the discrepancy between the different private sector forecasts reflects the degree of uncertainty concerning future economic change.

CHART A.17

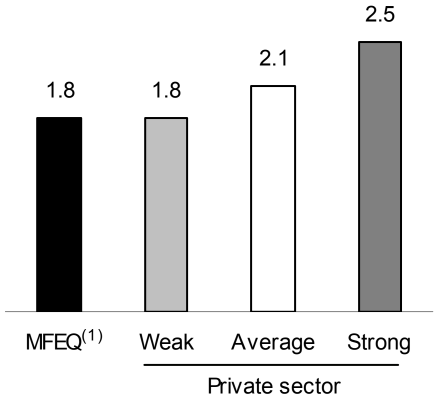
Economic growth in Québec in 2013
(real GDP, percentage change)



(1) Ministère des Finances et de l'Économie du Québec.
Source: Ministère des Finances et de l'Économie du Québec summary as of March 20, 2013, which includes the forecasts of 10 private sector institutions.

CHART A.18

Economic growth in Québec in 2014
(real GDP, percentage change)



(1) Ministère des Finances et de l'Économie du Québec.
Source: Ministère des Finances et de l'Économie du Québec summary as of March 20, 2013, which includes the forecasts of 10 private sector institutions.

TABLE A.3

Québec's economic outlook
(percentage change, unless otherwise indicated)

	2011	2012	2013	2014
Output				
Real gross domestic product	1.9	1.0	1.3	1.8
– *November 2012*	*1.7*	*0.9*	*1.5*	*2.0*
Nominal gross domestic product	4.7	3.4	3.6	3.9
– *November 2012*	*5.2*	*3.4*	*3.7*	*4.0*
Components of GDP (in real terms)				
Consumption	2.3	1.1	1.8	2.1
– *November 2012*	*2.0*	*1.4*	*1.8*	*2.0*
Government expenditures and investments	1.8	1.1	0.3	0.6
– *November 2012*	*0.4*	*0.4*	*0.4*	*0.6*
Residential investment	0.7	2.1	–4.6	–1.1
– *November 2012*	*1.5*	*1.4*	*–4.0*	*–1.1*
Non-residential business investment	6.6	7.6	2.0	3.7
– *November 2012*	*10.2*	*4.0*	*5.0*	*5.3*
Exports	–0.2	1.7	2.8	3.0
– *November 2012*	*2.1*	*0.9*	*2.8*	*3.3*
Imports	4.2	1.3	2.3	2.4
– *November 2012*	*4.0*	*1.7*	*1.9*	*2.6*
Labour market				
Job creation (thousands)	38.5	30.8	44.5	36.5
– *November 2012*	*38.5*	*24.8*	*41.6*	*38.4*
Unemployment rate (%)	7.8	7.8	7.5	7.4
– *November 2012*	*7.8*	*7.8*	*7.6*	*7.5*
Other economic indicators				
Nominal consumption	4.2	2.8	3.4	3.6
– *November 2012*	*3.6*	*2.9*	*3.2*	*3.7*
Wages and salaries	4.2	3.1	3.5	3.4
– *November 2012*	*4.1*	*2.9*	*3.4*	*3.5*
Net operating surplus of corporations(1)	6.1	–0.9	4.9	7.0
– *November 2012*	*11.8*	*1.7*	*7.0*	*8.5*
Consumer prices	3.0	2.1	1.6	1.9
– *November 2012*	*3.0*	*2.2*	*1.6*	*2.0*

(1) According to the new nomenclature used by Statistics Canada, the net operating surplus of companies includes, in particular, the profits and investment income of enterprises.
Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

1.9 Five-year economic outlook for 2013-2017

The five-year forecast of the Ministère des Finances et de l'Économie du Québec is comparable to that of the private sector regarding real GDP growth, price increases and nominal GDP growth.

— Real GDP is expected to grow at an average rate of 1.7% from 2013 to 2017, compared with the private sector forecast of 1.8%.

— Nominal GDP is expected to see an average growth rate of 3.7% from 2013 to 2017, identical to the private sector forecast.

TABLE A.4

Economic outlook for Québec – Comparison with the private sector
(percentage change)

	2013	2014	2015	2016	2017	Average 2013-2017
Real GDP						
Ministère des Finances et de l'Économie du Québec	1.3	1.8	1.9	1.9	1.7	1.7
Average private sector forecast	1.3	2.1	2.0	1.9	1.8	1.8
Price increases						
Ministère des Finances et de l'Économie du Québec	2.2	2.0	2.0	1.8	1.7	1.9
Average in the private sector	1.8	1.9	1.9	1.9	1.9	1.9
Nominal GDP						
Ministère des Finances et de l'Économie du Québec	3.6	3.9	3.9	3.7	3.5	3.7
Average in the private sector	3.1	4.0	3.9	3.8	3.7	3.7

Source: Ministère des Finances et de l'Économie du Québec summary as of March 20, 2013, which includes the forecasts of 10 private sector institutions.

2. THE SITUATION OF QUÉBEC'S MAIN ECONOMIC PARTNERS

Québec's economy is open to the world. While Québec has diversified trade in recent years, Canada and the United States are its main trading partners and their situation significantly affects the development of the Québec economy.

— Economic activity in Canada lagged in 2012 and growth stood at 1.8%, i.e. 0.1 percentage point below the November 2012 forecast. Growth in real GDP should reach 1.7% in 2013 and 2.2% in 2014, a downward adjustment of 0.2 and 0.1 percentage points, respectively, in relation to the November 2012 forecast.

— In the United States, after rising by 2.2% in 2012, real GDP should grow by 1.8% in 2013, then accelerate to 2.5% in 2014. Economic growth has thus been adjusted downward by 0.2 percentage point in 2013 in relation to what was forecast in November 2012.

The following sections focus on the economic outlook in Canada and the United States.

2.1 The economic situation in Canada

Economic activity in Canada lagged in 2012 and real GDP grew by 1.8%, i.e. 0.1 percentage point less than forecast in November 2012.

— Flagging consumption, persistent external turbulence and the fiscal adjustment measures under way affected the economy.

The outlook for the Canadian economy remains nonetheless positive. Growth in real GDP should reach 1.7% in 2013 and 2.2% in 2014.

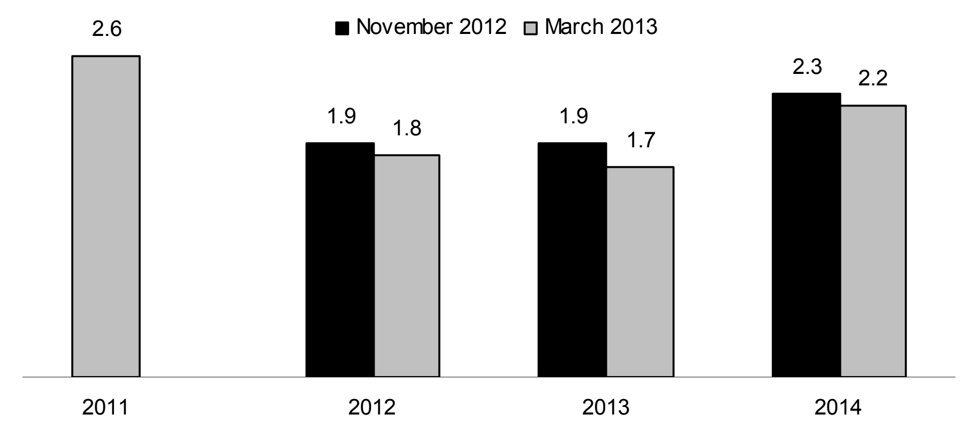
— Business investment and household consumption expenditures will continue to sustain economic activity.

— Moreover, the gradual improvement in the global economy will further stimulate Canadian exports.

On the other hand, the Canadian residential sector has entered a downturn. In addition, the pursuit of control of government spending in a context where several provinces and the federal government are seeking to restore or maintain fiscal balance will limit economic growth.

CHART A.19

Economic growth in Canada
(real GDP, percentage change)



Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

❑ Household consumption and labour market

Following a 1.9% increase in 2012, real consumer spending should rise by 2.2% in 2013 and 2.4% 2014. A strong labour market will sustain household spending.

— After a gain of 201 500 jobs in 2012, 164 500 new jobs should be created in 2013 and 201 600 jobs in 2014, an average annual increase of 1.1% over the three years.

— Solid labour market performance led to a gradual reduction in the unemployment rate, which fell from 8.3% in 2009 to 7.2% in 2012. With ongoing job creation, the Canadian unemployment rate will continue to improve, from 7.2% in 2013 to 7.1% in 2014.

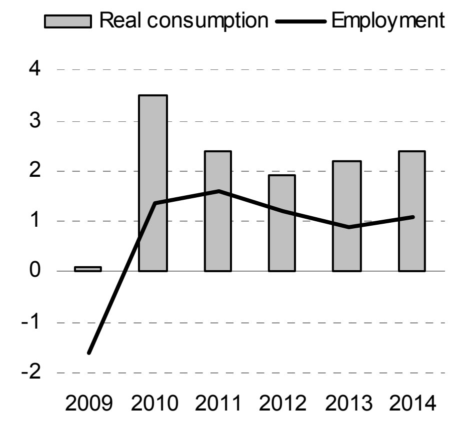
❑ Residential construction investment

While low interest rates are helping to support demand, the new measures implemented by the federal government to limit mortgage debt in Canada will dampen activity in the residential sector.

— Following a 5.8% increase in 2012, residential investment should fall by 5.8% in 2013 and 2.0% in 2014.

CHART A.20

Job creation and consumer spending in Canada
(percentage change)

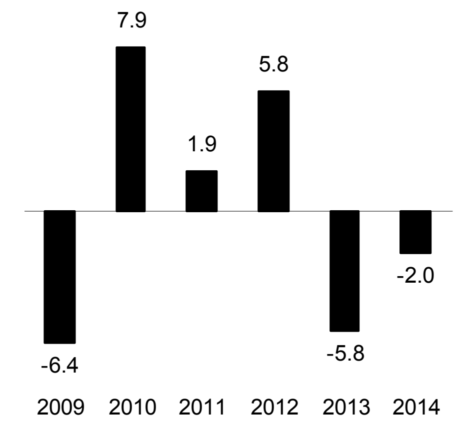


Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.21

Residential investment in Canada

(percentage change, in real terms)



Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

❑ Non-residential business investment

Business investment rose at a sustained pace, i.e. 11.3% in 2011 and 7.2% in 2012, in nominal terms.

— The value of non-residential business investment should continue to experience robust growth and increase by 4.6% in 2013 and 5.6% in 2014.

Business investment will remain an engine of economic growth in Canada. Indeed, businesses continue to benefit from a favourable environment, in particular low interest rates, healthy balance sheets and a strong Canadian dollar, which reduces the cost of imported machinery.

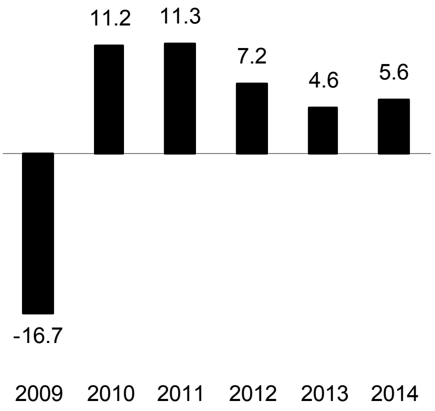
❑ Government investments

Growth in public spending will be weak in the coming years. In order to restore fiscal balance, the federal government and provincial governments have adopted expenditure control policies.

— Accordingly, after declining in 2011 and 2012, the value of government investments should increase by only 1.5% in 2013 and 2.1% in 2014. This growth will nonetheless maintain a high level of public investment in relation to the 2000s.

CHART A.22

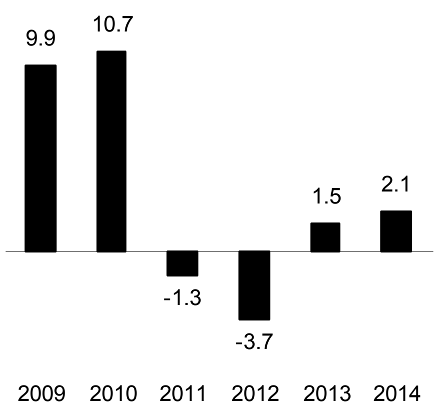
Non-residential business investment in Canada
(percentage change, in nominal terms)



Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.23

Government investments in Canada
(percentage change, in nominal terms)



Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

❑ External trade

Canadian exports experienced a slowdown in 2012 against a backdrop of lower worldwide demand for Canadian products. Growth will remain modest in 2013 and pick up in 2014, in particular with the anticipated upturn in growth in the U.S. economy.

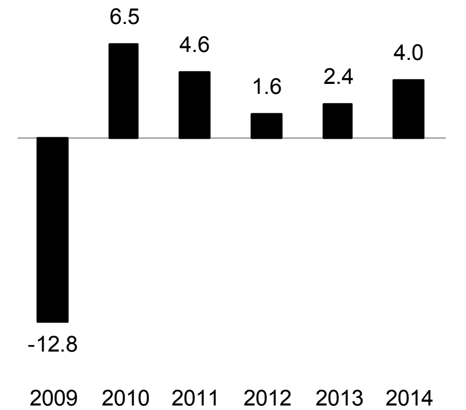
— Accordingly, exports should increase by 2.4% in 2013 and 4.0% in 2014.

On the other hand, increased imports will mitigate the impact of growth in exports. As a result, external trade should contribute only slightly to economic growth in Canada in 2013 and 2014.

CHART A.24

Canadian exports

(percentage change, in real terms)

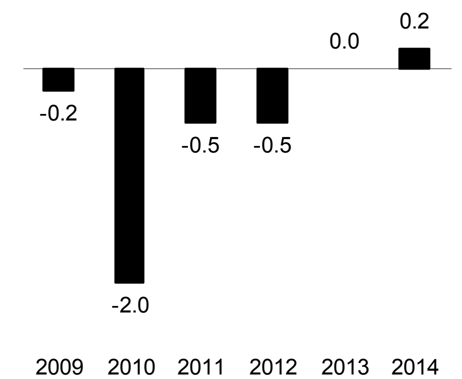


Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

CHART A.25

Contribution of net exports to Canada's economic growth

(in percentage points)



Sources: Statistics Canada and Ministère des Finances et de l'Économie du Québec.

❑ Abundant oil means advantageous prices in North America

Since November 2012, the price of Brent oil has hovered around US$110 per barrel.

It should average US$106 in 2013 and US$103 in 2014. As for the price of WTI oil, it will reach around US$90 on average this year and US$87 in 2014.

— The gap between the prices of Brent and WTI oil should persist in the coming two years despite increased oil pipeline capacity intended to reduce oil surpluses in the U.S. Midwest.

— Furthermore, Canadian heavy crude oil, the Western Canada Select, will continue to sell for roughly US$50 per barrel less than Brent oil, in particular because of insufficient pipeline transmission capacity, which is limiting outlets for Canadian production.

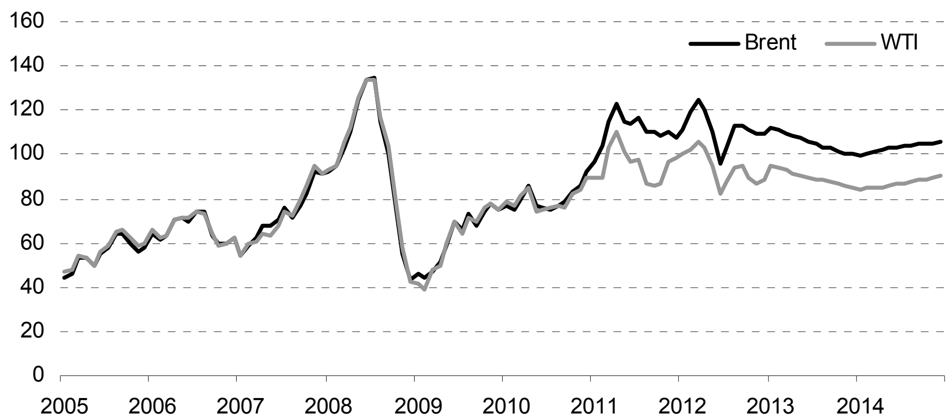
In 2013 and 2014, worldwide supply should outstrip demand because of an increase mainly from non-member countries of the Organization of Petroleum Exporting Countries (OPEC), including the United States.

— Indeed, oil production in the United States will exceed 7 million barrels per day in 2014.

Moreover, growth in demand for oil should remain moderate in the short term because of the difficulties that the advanced economies are still facing. This weakness will be partially offset by stronger growth in consumption in the emerging economies.

CHART A.26

Price of Brent and WTI oil
(U.S. dollars per barrel, monthly averages)



Sources: Bloomberg and Ministère des Finances et de l'Économie du Québec.

❑ The Canadian dollar

The Canadian dollar is expected to remain close to parity with the U.S. dollar. It should stand at an average of 98.8 U.S. cents in 2013 and 99.6 cents in 2014.

In 2012, the loonie remained on average at parity with the greenback, at 100.1 U.S. cents. It nonetheless fluctuated during the year, affected by movements in commodities prices and turbulence on financial markets.

— From mid-November 2012 to the end of January 2013, the dollar remained above parity then slid below parity in the wake of the announcement by the Bank of Canada that monetary tightening should begin later than previously indicated.

The Canadian dollar should continue to hover below parity with the U.S. dollar in the coming quarters, a reflection of falling oil prices.

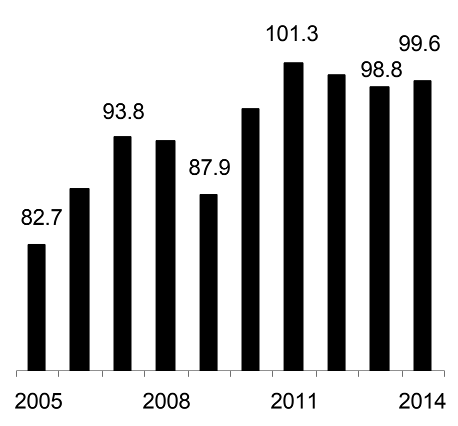
The Canadian dollar will nonetheless be supported by demand from foreign investors for Canadian assets, owing in particular to:

— the appeal of Canadian government bonds: Canada is one of the rare countries in the world assigned the highest credit rating with stable outlook by the main credit-rating agencies;

— positive spreads between short-term interest rates in Canada and the United States as a result of Canada's slightly more restrictive monetary policy.

CHART A.27

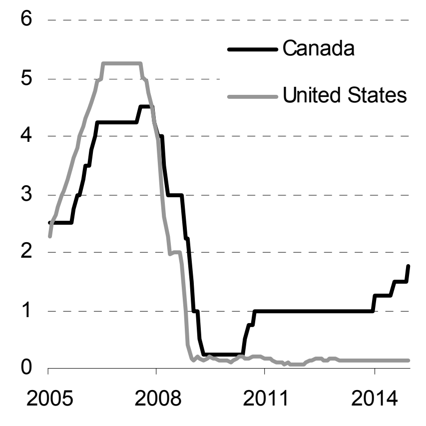
Canadian dollar exchange rate
(annual averages, in U.S. cents)



Sources: Bloomberg and Ministère des Finances et de l'Économie du Québec.

CHART A.28

Key interest rate
(per cent)



Sources: Statistics Canada, Bloomberg and Ministère des Finances et de l'Économie du Québec.

❑ Cautious optimism on financial markets

The uncertainty that prevailed on financial markets in late 2012, especially arising from the negotiations in the U.S. Congress concerning the "fiscal cliff," spurred investors to increase their demand for sound assets, including Canadian sovereign bonds.

In early 2013, growing optimism about worldwide economic prospects was observed on financial markets.

This optimism led to renewed interest among investors for riskier assets. Investors began to abandon safer assets such as Canadian sovereign bonds in favour of equities or other riskier bonds, which led, in particular, to an increase in yields on the Canadian bond market.

— Accordingly, after declining to 1.78% on average in December 2012, yield on Canadian 10-year bonds increased to 1.97% in February 2013.

However, the global economic environment remains fragile and financial markets are still prone to episodes of volatility. These factors will sustain demand for bonds.

— Consequently, against a backdrop of expansionist worldwide monetary policy, bond rates will only increase very gradually.

— The yield on federal 10-year bonds should be 2.3% on average in 2013 and 3.2% in 2014.

Bearing in mind that growth in Canada should continue to be modest and the outlook for inflation is to be contained, the Bank of Canada will remain accommodating for a prolonged period. It should only tighten its monetary policy very gradually in 2014.

TABLE A.5

Canadian financial markets
(percentage rate)

	2011	2012	2013	2014
Target overnight rate	1.0	1.0	1.0	1.4
– *November 2012*		*1.0*	*1.0*	*1.4*
3-month Treasury Bills	0.9	1.0	1.0	1.4
– *November 2012*		*1.0*	*1.0*	*1.4*
10-year bonds	2.8	1.9	2.3	3.2
– *November 2012*		*1.9*	*2.4*	*3.2*
Canadian dollar (in U.S. cents)	101.3	100.1	98.8	99.6
– *November 2012*		*100.7*	*99.1*	*100.7*

Sources: Statistics Canada, Bloomberg and Ministère des Finances et de l'Économie du Québec.

2.2 The economic situation in the United States

❑ Gradual strengthening of economic growth

After gaining 2.2% in 2012, real GDP in the U.S. is expected to grow by 1.8% in 2013 and then accelerate to 2.5% in 2014.

— Economic growth has thus been revised downward by 0.2 percentage point in 2013 compared with what was forecast in November 2012.

This adjustment is attributable in particular to the very slow pace of economic activity in the last quarter of 2012, stemming essentially from short-lived factors. Nonetheless, the U.S. economy should continue to grow, but at a modest pace in the first half of 2013. It will afterwards recover gradually.

In 2013 and 2014, U.S. economic activity should be sustained chiefly by consumption, business investment and the housing sector, which began a sustainable recovery in 2012.

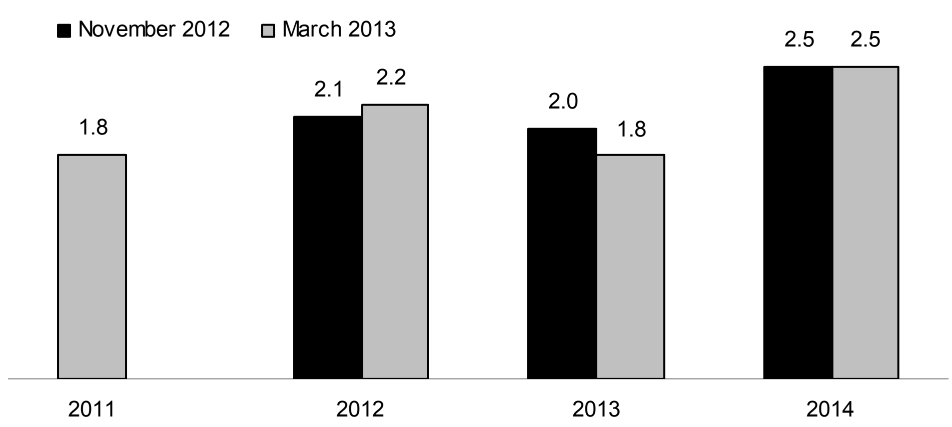
On the other hand, the impact of the federal government's fiscal and budgetary consolidation, which will be necessary to rebalance U.S. public finances, is expected to be the main drag on economic growth.

— The restrictive fiscal and budgetary measures adopted in early 2013 should represent 1.5% of GDP in 2013. Restraint will be slightly less in 2014.

Moreover, the still-fragile global economic environment in 2013 should continue to limit the external sector's contribution to economic growth.

CHART A.29

Economic growth in the United States
(real GDP, percentage change)



Sources: IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

❑ Growth in consumption limited by fiscal consolidation

Consumption should continue to grow modestly, gaining 1.8% in 2013 and accelerating to 2.2% in 2014.

Growth in consumer spending will be affected in 2013, as fiscal consolidation measures adopted by Congress following negotiations on the fiscal cliff take effect. These measures include in particular the expiry of the reduced rate for employee contributions to Social Security, which will limit growth in disposable income.

— Accordingly, personal disposable income should decline in the first quarter of the year and then gradually recover, gaining 1.0% in 2013 and 2.9% in 2014.

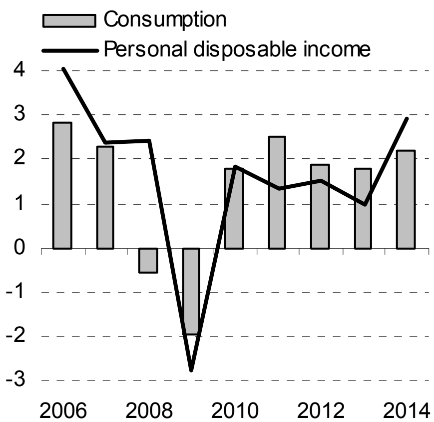
Still, the medium-term outlook for growth in U.S. household consumption is favourable. Over the last two years, households have substantially improved their financial situation, allowing them to spend more despite lower government transfers and higher taxes.

In addition, labour market's gradual but sustained firming will lead to a drop in the unemployment rate and improved consumer confidence, factors that will also support consumption.

— Job creation will amount to 2.0 million in 2013 and 2.4 million in 2014, i.e. gains of 1.5% and 1.7% respectively.

CHART A.30

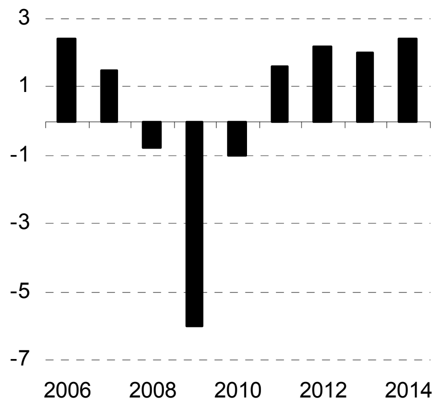
Income and consumption
(percentage change, in real terms)



Sources: IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

CHART A.31

Job creation
(millions)



Sources: IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

A notable improvement in the private sector's balance sheet

During the years leading up to the recession, households and businesses took on large amounts of additional debt.

- Household debt as a percentage of personal disposable income exceeded 131% in 2007, while business debt as a percentage of net equity stood at 82% in 2008.

However, this trend was reversed by the bursting of the real estate bubble in 2006 and the ensuing recession.

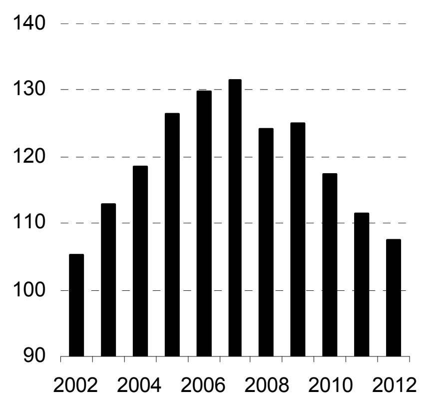
- Household debt as a percentage of personal disposable income has fallen significantly since 2007, reaching 106% in late 2012, its lowest level since 2002.
- At the same time, business debt as a percentage of net equity fell to 69% in 2011, the lowest since 2006.

On the other hand, the deficit of the U.S. federal government rose from 1.2% of GDP in 2007 to 7.0% in 2012 because of the significant economic recovery plans put in place to counter the effects of the recession and to support the recovery.

Recently, the U.S. Congress has indicated that it wants to restore balance to U.S. public finances. The private sector's currently more favourable financial situation will help support economic growth, offsetting the impact of government budgetary restrictions over the coming years.

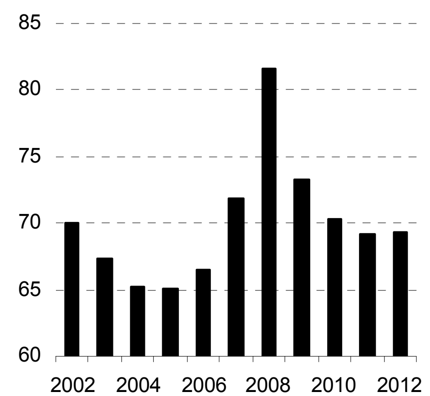
- In addition, the recovery on the labour market and in the housing sector will support consumer spending and enable businesses to continue expanding, despite the tax increases and spending reductions needed to reduce the federal government's deficit.

Household debt
(as a percentage of personal disposable income)



Source: IHS Global Insight.

Business debt
(as a percentage of net equity, non-financial businesses)



Source: IHS Global Insight.

❑ Sustainable recovery in the real estate sector

After impeding economic growth for many years, the housing sector has entered a sustainable recovery. Residential investment rose by 12.1% in real terms in 2012, the first increase since 2005.

— Residential investment should accelerate in the coming years, reaching 14.8% in 2013 and 15.7% in 2014.

House prices have also been in an uptrend since early 2012. They are rising because of higher demand for properties as well as the depletion of excess inventories of homes for sale, which have fallen to their lowest point in more than seven years.

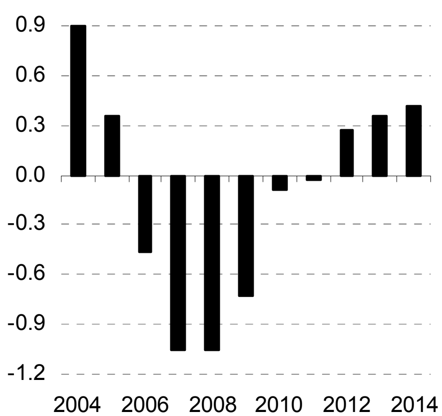
This price increase, together with the improved labour market and households' healthier financial situation, has fostered a significant increase in new construction.

— Accordingly, in late 2012, housing starts hit their highest point since 2008.

— They are expected to continue rising, averaging 1.0 million units in 2013 and 1.3 million in 2014.

CHART A.32

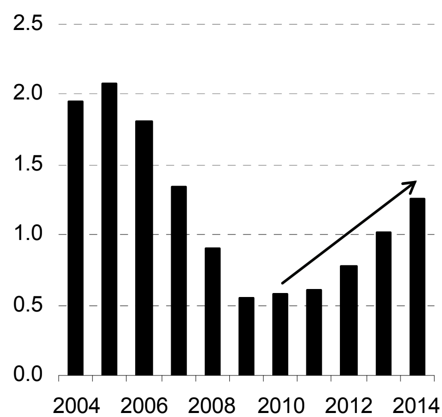
Contribution of the housing sector to real GDP growth
(percentage points)



Sources: IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

CHART A.33

Housing starts
(millions of units)



Sources: IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

❑ Favourable conditions for business investment in the United States

Following a gain of 7.7% in 2012, business investment should grow by 4.8% in 2013 and 6.2% in 2014.

American businesses increased their investments substantially in 2012 despite the uncertainties surrounding negotiations over restoring fiscal balance and an international situation that remains difficult.

Investment should continue to grow in 2013 and 2014, supported by an accommodating monetary policy that enables businesses to obtain financing at very attractive rates.

— In addition, businesses have had access to an accelerated depreciation program in recent years, which has stimulated investment, notably in equipment and software. This measure was renewed under the agreement Congress reached on January 2, 2013.

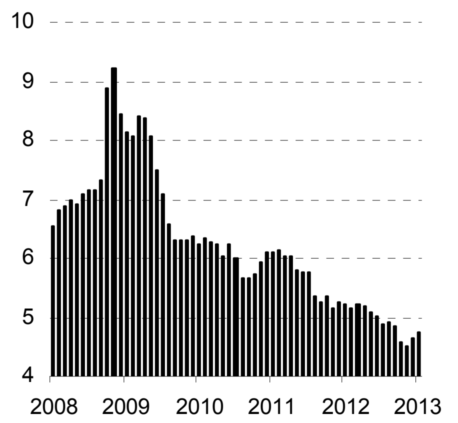
The expected growth in business investment should enable it to return to its pre-recession level in 2013.

Moreover, the strength of the energy sector in the United States, which is already resulting in affordable energy prices, could become an important comparative advantage for the U.S. industrial sector over the coming years.

— Abundant energy could help encourage manufacturing companies to locate in the U.S. and increase production there, representing a major change after a long period of off-shoring production to economies featuring low labour costs.

CHART A.34

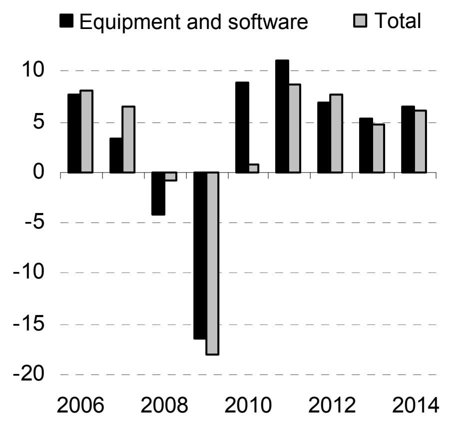
Rates of corporate bonds(1)
(per cent)



(1) Corporate bonds rated Baa by Moody's.
Source: IHS Global Insight.

CHART A.35

Business investment
(percentage change, in real terms)



Sources: IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

❑ The government sector will limit economic growth

After the last recession, the budget deficit of the U.S. federal government rose sharply, reaching a peak of 10.1% of GDP in 2009. It has since fallen, declining to 7% of GDP in 2012.

This drop in the federal deficit stems in part from restrictions on spending, which declined by 2.8% in 2011 and 2.2% in 2012 in real terms. However, these restrictions at the federal level will become more intense over the coming years in order to achieve a more substantial reduction in the deficit to GDP ratio.

— Real spending by the U.S. federal government will fall by 5.0% in 2013 and 4.8% in 2014.

Because of the substantial cuts to the federal government's spending in 2013 and 2014, spending by all levels of government should continue to fall in real terms.

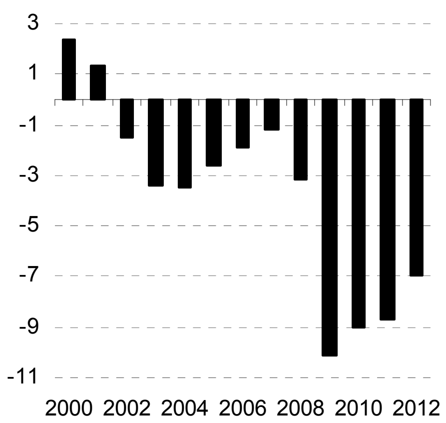
— Accordingly, following a decline of 1.7% in 2012, real spending by all levels of government is expected to fall by 2.3% in 2013 and 1.8% in 2014, which will continue to limit economic growth.

For its part, the U.S. Federal Reserve should maintain a very accommodating monetary policy for an extended period and continue its asset purchase programs to support economic activity.

— It recently revealed its commitment to maintain an expansionist monetary policy at least as long as the unemployment rate remains above 6.5% and inflation expectations are below 2.5%.

CHART A.36

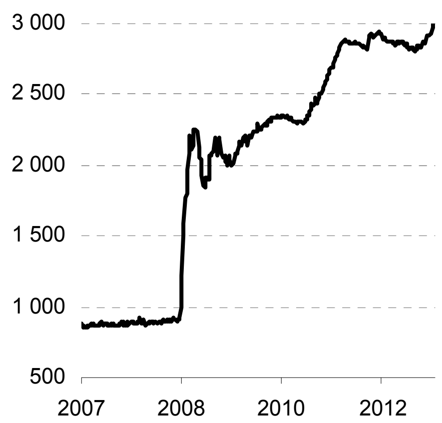
Federal government deficit
(as a percentage of nominal GDP)



Source: Office of Management and Budget.

CHART A.37

U.S. Federal Reserve balance sheet
(billions of U.S. dollars)



Source: U.S. Federal Reserve.

Automatic spending cuts at the U.S. federal government

Under existing law, substantial U.S. federal government spending cuts came into effect on March 1, 2013.

- These spending cuts, called "the sequester", are intended to reduce the budget allocated to a broad array of government programs by US$85 billion between March 1 and September 30, 2013, when the 2013 fiscal year ends.
- For subsequent fiscal years, these cuts will amount to US$110 billion annually. They are intended to reduce the deficit by $1.2 trillion from 2013 to 2021, including the savings generated by lower debt service.

Origins and definition of the sequester

The legislative provisions relating to the sequester originate in the agreement on raising the debt ceiling, reached in August 2011.

- The agreement on raising the debt ceiling (*Budget Control Act*) stipulated that, unless a deficit reduction plan totalling at least US$1.2 trillion between 2013 and 2021 was passed by January 15, 2012, an equivalent sequester would be triggered as of January 2, 2013.
- As stipulated in the *Budget Control Act*, half of the automatic cuts must affect programs associated with defence, while the other half will affect discretionary spending.
  - The law thus protects spending associated with Medicaid, old age security and food stamps programs.
  - However, it leaves the government little leeway in how the cuts are to be implemented.

Economic impact

The "fiscal cliff" agreement reached on January 2, 2013 delayed the effective date of the sequester by two months, to March 1, 2013.

- Accordingly, the budget allocated to federal agencies is reduced by US$85 billion for fiscal year 2013 and by US$110 billion for fiscal year 2014, leading to a drop in the federal government's effective spending of about US$65 billion for calendar year 2013, i.e. 0.4% of GDP.[1]

These spending cuts are in addition to the tax increases adopted in January 2013 as part of the fiscal cliff agreement.

- Taken as a whole, these measures, which total 1.5% of GDP in 2013, will limit consumption, investment and employment.

1 The reduction in the allocated budget does not necessarily result in an equivalent spending reduction in the same year, since the government may incur in the year spending it committed to in prior years.

❑ Gradual progress in the external sector

Slowing growth of emerging economies and the ongoing difficulties in the euro area limited the external sector's contribution to U.S. economic growth in 2012.

— However, exports gained 3.3% in real terms, exceeding growth in imports, which amounted to 2.4%.

Over the coming years, the gradual recovery of economic activity in the euro area and a relatively weak U.S. dollar should provide support for international demand for American products.

— Accordingly, real U.S. exports are expected to rise by 2.6% in 2013 and 6.4% in 2014.

Moreover, the improvement in household consumption stemming from gains in employment, as well as continued business investment, should also stimulate imports.

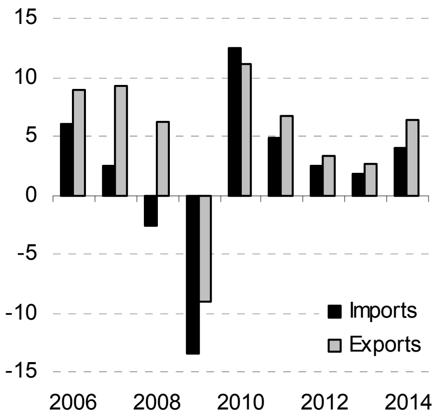
— Consequently, growth in real imports should amount to 1.7% in 2013 and then accelerate to 3.9% in 2014.

Because growth in exports will exceed that in imports, the trade deficit will fall moderately, to 2.9% of GDP in real terms in 2013 and 2.6% in 2014.

CHART A.38

Exports and imports

(percentage change, in real terms)

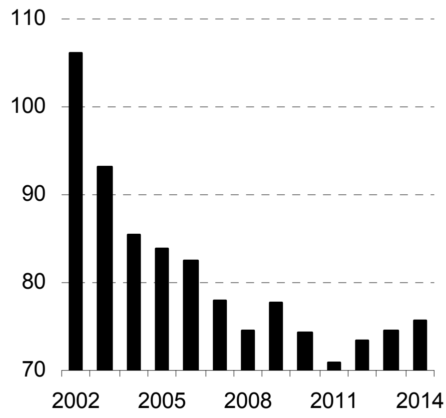


Sources: IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

CHART A.39

Weighted exchange rate of the U.S. dollar

(index,[1] March 1973 = 100)



(1) Index weighted by trade with major trading partners.
Sources: IHS Global Insight and Ministère des Finances et de l'Économie du Québec.

Change in the U.S. trade balance for oil products

Over the last few years, the United States trade deficit as a percentage of GDP has improved, falling in real terms from over 6% of GDP in 2005 to 4.2% in 2012.

This decline is largely attributable to the improved trade balance in oil products, stemming in particular from the energy revolution currently underway in the United States.

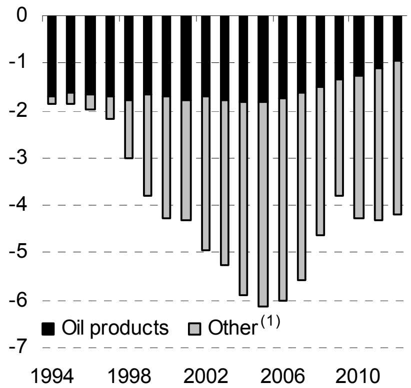
- In real terms, exports of oil products have been trending up since 2006, while imports of these products have been declining.
- Imports of crude oil, which peaked at 3 821 million barrels in 2004, fell to 3 094 million barrels in 2012.

Imports of oil products accounted for more than 25% of total imports in 1994, compared with 10.6% today. On the other hand, oil products' share of total exports has risen from 4.1% in 1994 to 5.3% in 2012.

- Consequently, the trade deficit attributable to the oil products sector, which accounted for more than 92% of the total trade deficit in 1994, has fallen significantly, amounting to almost 23% of the total deficit in 2012.
- Moreover, U.S. production of crude oil, according to the Energy Information Administration, should rise from 5.5 million barrels per day in 2010 to 7.2 million in 2014, a gain of more than 31%.

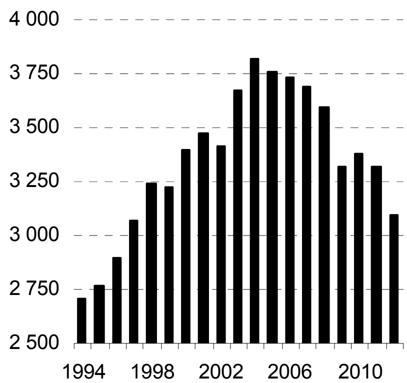
This increase in domestic production results from new techniques for extracting oil from shale rock. Because of these techniques, the United States could become self-sufficient in oil over the coming years.

U.S. trade deficit
(as a percentage of GDP, in real terms)



(1) Non-oil products and statistical adjustments
Source: United States Census Bureau.

Annual crude oil imports
(millions of barrels)



Source: United States Census Bureau.

3. THE INTERNATIONAL ECONOMIC CONTEXT

This section describes the international economic outlook. After reaching 3.0% in 2012, global economic growth should gradually accelerate to 3.2% in 2013 and 3.7% in 2014.

— Global growth has been revised downward by 0.1 percentage point in 2013 compared with what was forecast in November 2012. There is no change for 2014.

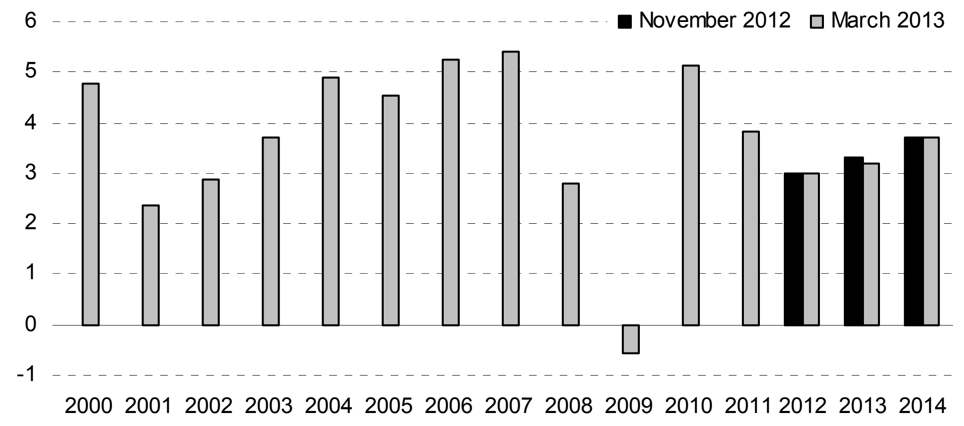
The slower pace of global growth in 2012 is attributable to weak activity in the advanced economies, chiefly the euro area, which has also led to a slowdown in emerging economies.

— Many advanced economies entered into recession in 2012, including the euro area, the United Kingdom and Japan, while growth in the United States was limited by uncertainties over Congressional negotiations on the fiscal cliff.

— In emerging economies, the slower pace of growth chiefly resulted from weakening demand in the advanced economies, but also from specific domestic difficulties.

CHART A.40

Global economic growth
(real GDP based on purchasing power parity, percentage change)



Sources: IHS Global Insight, International Monetary Fund and Ministère des Finances et de l'Économie du Québec.

❑ Uncertainty gradually abating

Some of the major risks present in 2012 have abated. In the United States, the fiscal cliff has largely been avoided. In Europe, the measures taken to secure the viability of the euro area have partially eased tensions on financial markets.

— The European Central Bank's announcement in the summer of 2012 concerning its sovereign bond purchasing program contributed significantly to this period of calm.

However, the uncertainty generated by the economic and budgetary issues in the euro area is still substantial and will abate only gradually. On the other hand, the situation in emerging economies appears to have stabilized, particularly in China, with a slight rebound in growth in the last quarter of 2012, while leading indicators are giving encouraging signs.

The global growth outlook should thus improve gradually during 2013. Global growth will continue to gather pace in 2014.

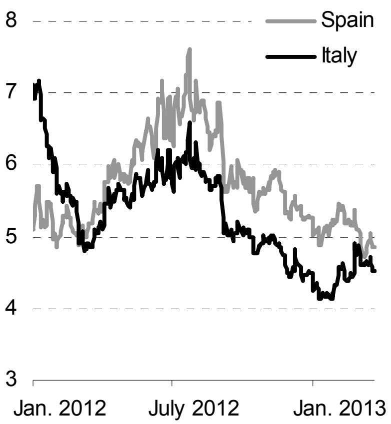
— In the euro area, the recession is expected to continue in 2013, but the economic situation should begin to stabilize during the year and this process will continue in 2014.

— In the United States, growth is expected to remain modest in 2013, limited by weak expansion in real GDP early in the year, but the pace of growth is expected pick up over the ensuing semesters.

CHART A.41

Yields on 10-year sovereign bonds

(per cent)

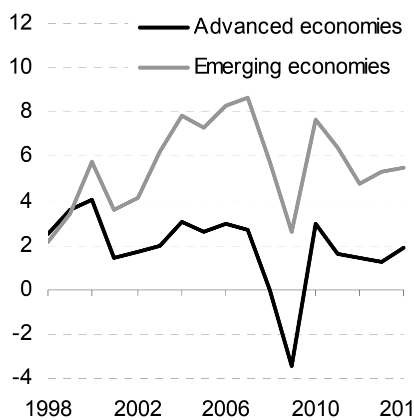


Source: Bloomberg.

CHART A.42

Growth in advanced and emerging economies

(real GDP based on purchasing power parity, percentage change)



Sources: IHS Global Insight, International Monetary Fund and Ministère des Finances et de l'Économie du Québec.

3.1 The advanced economies will overcome their difficulties very gradually

After reaching 1.4% in 2012, growth in the advanced economies should continue at a modest rate of 1.2% in 2013 and then reach 1.9% in 2014. This outlook stems from the deep-seated difficulties some of these economies continue to deal with, difficulties that will be overcome only gradually starting in the second half of 2013.

— In the euro area, economic and budgetary issues reflected in a record unemployment rate and restricted access to credit will continue to weigh on domestic demand. Consumer spending will also suffer as a result of continued austerity measures, though their impact is not as great as in the past.

— In the United States, the tax increases and spending cuts that took effect in the first quarter of 2013 should affect economic growth in the first half of 2013 and their impact should moderate thereafter.

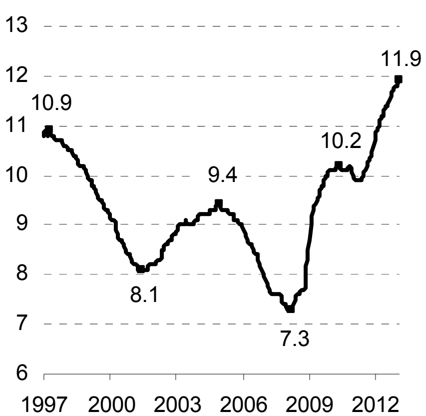
— In Japan, the economy experienced a sharp decline in the second half of 2012, particularly under the impact of the drop in exports.

Nonetheless, activity in the advanced economies should recover gradually, fostered by very accommodating monetary policy, easing financial tensions and firmer global demand. In Japan, the economy will be supported by the government's ambitious stimulation plan.

CHART A.43

Unemployment rate in the euro area

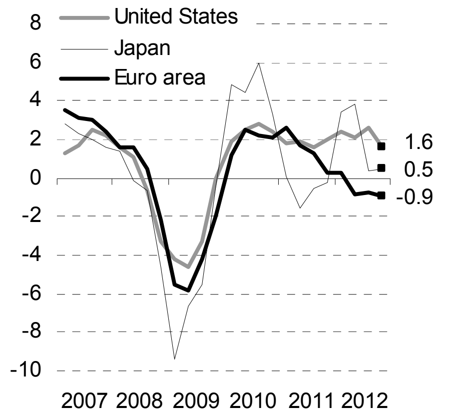
(per cent)



Source: Eurostat.

CHART A.44

Growth in the United States, Japan and euro area
(quarterly real GDP, annual percentage change)



Sources: Datastream and IHS Global Insight.

❑ Euro area governments are making structural reforms

In recent years, the governments of countries under stress in the euro area, such as Portugal, Ireland, Italy, Greece and Spain, have adopted structural reforms to correct macroeconomic imbalances and improve their economic competitiveness.

For some, such reforms were a condition for receiving assistance from the International Monetary Fund and the European Union. These reforms target in particular the labour market and regulation of the market for goods and services.

- The labour market reforms aim in particular to foster greater flexibility in employment conditions so that companies can more easily adapt to business cycles. They are also aimed at increasing labour market participation. Accordingly:
  - Spain has allowed companies to modify labour contracts once their revenue has fallen for two quarters;
  - Italy has raised the retirement age and set a timetable for standardizing conditions for men and women. Currently, women can receive retirement benefits sooner than men.
- Reforms to the market for goods and services are designed in particular to increase the private sector's presence in the economy and reduce regulatory barriers to competition. Accordingly:
  - Greece has liberalized road transport, Ireland has announced the partial privatization of electricity and gas companies and Portugal has liberalized regulated professions.

It is difficult to assess with accuracy the impact of these reforms. Still, the resulting adjustments should support firmer medium-term and long-term economic growth in the euro area.

TABLE A.6

Structural reforms: measures taken between 2010 and 2012

	Portugal	Ireland	Italy	Greece	Spain
Labour market					
– Reforms of the unemployment allowance and social protection	X	X	X	X	X
– Reforms of labour market regulation	X		X	X	X
Market for goods and services					
– Privatizations and reduction of the regulatory burden	X	X	X	X	X

Sources: Organization for Economic Cooperation and Development and International Monetary Fund

Strengthened economic governance in the euro area

The emergence of the sovereign debt crisis in the euro area in 2009 highlighted the macroeconomic disparities that had arisen among member states over the previous years.

- On average, from 2004 to 2008, labour productivity in Spain was 36% below that of the euro area's group of five leading countries in that regard. This gap was 27% for Italy and 64% for Portugal.
- This lower level of competitiveness contributed to a deteriorating trade balance that stood at –6.7% of GDP in 2007 in Spain, –10.1% of GDP in 2008 in Portugal and –2.0% of GDP in 2010 in Italy.

These disparities have put the monetary union's stability at risk. In response, European authorities set up in December 2011 a legislative framework to better monitor certain macroeconomic parameters and bolster application of recommendations on structural reforms by the European Commission (EC).

- Within this framework, the EC will regularly monitor indicators on competitiveness, unemployment, credit, asset prices and external trade.

This heightened level of macroeconomic oversight is one of the pillars of the euro area's new governance, which also seeks to ensure greater fiscal discipline. Measures adopted in this sense include:

- the requirement that governments present their draft budget in October of each year, based on independent macroeconomic forecasts;
- the EC's authority to analyze national budgets and require adjustments if they do not comply with European rules;
- more automatic application of sanctions where a member state fails to comply with the timetable set for the reduction of its debt load, if allowed by its economic situation.

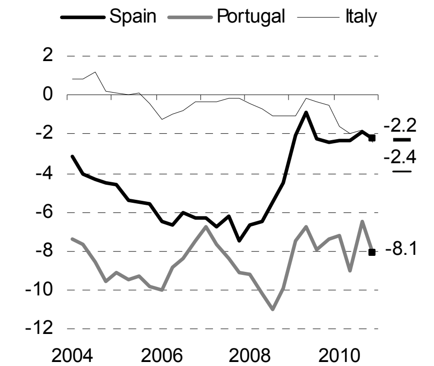
GDP per hour worked
(average level over the period, real value in euros)

	Average, 2004-2008
Group of the five most productive countries in euro area	**44**
Gap compared to this group:	
– Spain	–36%
– Italy	–27%
– Portugal	–64%

Sources: Eurostat and Ministère des Finances et de l'Économie du Québec.

Trade balance

(as a percentage of GDP, quarterly data)



Sources: Eurostat and Ministère des Finances et de l'Économie du Québec.

3.2 Activity in emerging economies is rebounding

Economic growth in the emerging economies slowed in 2012 with real GDP gaining 4.8% following growth of 6.4% in 2011. Growth in emerging economies is expected to recover over the next two years, reaching to 5.3% in 2013 and 5.5% in 2014.

— Monetary easing and economic support policies adopted over the last few quarters will help support economic activity in many of these countries. For example:

  — the Chinese government has undertaken to stimulate investment by adopting a major infrastructure investment plan;

  — in Brazil, growth will be stimulated by the positive impact of the significant monetary easing adopted previously as well as by infrastructure construction relating to major sporting events, namely the 2014 FIFA World Cup and the 2016 Summer Olympic Games.

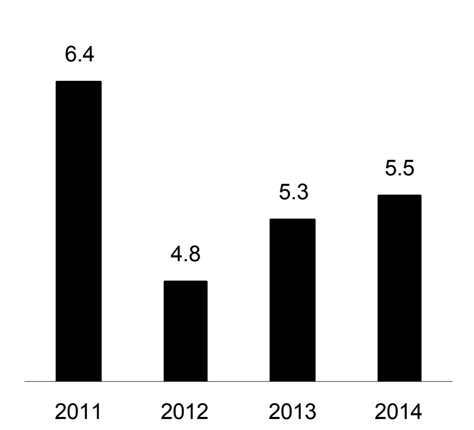
— In addition, the gradual recovery in global demand will help to firm up the exports of emerging economies.

There have been recent signs of firming economic activity, especially in China, where exports are recovering and industrial production is accelerating.

— Chinese exports surged more than 20% year over year since January 2013 and growth in industrial production has been accelerating since the summer of 2012. It has been roughly 10% since late 2012.

CHART A.45

Growth in emerging economies
(real GDP based on purchasing power parity, percentage change)

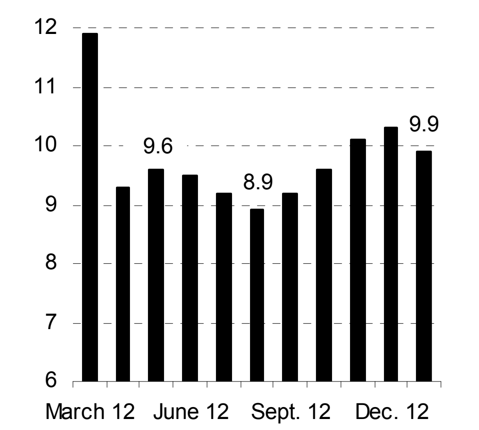


Sources: IHS Global Insight, International Monetary Fund and Ministère des Finances et de l'Économie du Québec.

CHART A.46

Chinese industrial production[(1)]

(annual percentage change)



(1) The last figure represents the average of the first two months of 2013.
Source: Bloomberg.

❑ Gradual recovery in global trade

Along with the global economic slowdown, growth in world trade decelerated in 2012, amounting to 2.8%, following a rebound to 12.6% in 2010 and a gain of 5.9% in 2011.

Trade flows were affected in 2012 by weak activity in the advanced economies, particularly in Europe, the world's main trading bloc, but also by slower growth in emerging economies.

— The euro area's imports of merchandise fell 3.4% in 2012, while its exports grew by only 0.3%.

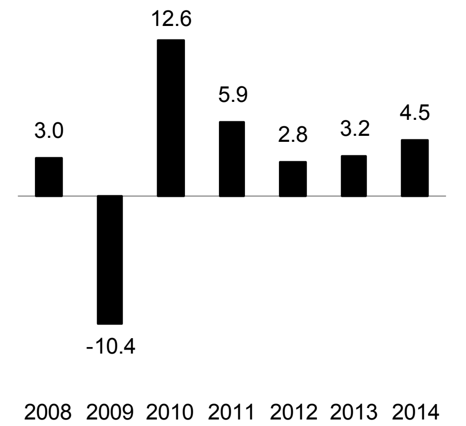
However, world trade is expected to recover modestly in the first half of 2013, thanks to the already tangible acceleration in activity in emerging economies. It should speed up even more in the second half of 2013 and in 2014, reflecting the gradual improvement in economic conditions in the euro area and the United States.

— Accordingly, in real terms, global exports should gain 3.2% in 2013 and 4.5% in 2014.

— Moreover, the most recent monthly data on world trade already show a recovery in exports from emerging economies in late 2012, more particularly in Asia.

CHART A.47

World exports of goods and services
(percentage change, in real terms)



Sources: IHS Global Insight, International Monetary Fund and Ministère des Finances et de l'Économie du Québec.

CHART A.48

Exports of merchandise from Asian emerging economies
(percentage change, in real terms)

Note: The change is calculated using the average of the last three months over that of the preceding three months.
Sources: CPB Netherlands Bureau for Economic Policy Analysis and Ministère des Finances et de l'Économie du Québec.

3.3 Outlook by country

In **Canada**, while growth slowed in the second half of 2012, the economic outlook remains positive. Economic activity should be supported by household consumption and business investment. However, budget restraint by the various orders of government and a slowdown in residential investment should limit growth. Accordingly, real GDP is expected to grow by 1.7% in 2013 and 2.2% in 2014.

In the **United States**, growth is expected to decline from 2.2% in 2012 to 1.8% in 2013, because of factors that are mainly temporary. It will recover during 2013, once fiscal and budgetary policies aimed at reducing the deficit become clearer. Growth in economic activity should accelerate to 2.5% in 2014. The growth outlook in the United States is positive in the medium term, in particular because of the strength of the country's energy sector.

TABLE A.7

Global economic growth outlook
(real GDP, percentage change)

	Weight in global GDP(1)	2012	2013	2014
World(2)	**100.0**	**3.0**	**3.2**	**3.7**
– *November 2012*		*3.0*	*3.3*	*3.7*
Advanced economies(2)	**50.5**	**1.4**	**1.2**	**1.9**
– *November 2012*		*1.3*	*1.3*	*1.9*
Canada	1.8	1.8	1.7	2.2
– *November 2012*		*1.9*	*1.9*	*2.3*
United States	19.1	2.2	1.8	2.5
– *November 2012*		*2.1*	*2.0*	*2.5*
Euro area	14.1	–0.6	–0.4	0.5
– *November 2012*		*–0.7*	*–0.2*	*0.7*
United Kingdom	2.9	0.2	0.9	1.3
– *November 2012*		*–0.1*	*0.9*	*1.3*
Japan	5.6	2.0	1.1	1.2
– *November 2012*		*2.1*	*0.9*	*1.4*
Emerging economies(2)	**44.7**	**4.8**	**5.3**	**5.5**
– *November 2012*		*4.9*	*5.4*	*5.6*
China	14.3	7.8	8.0	7.8
– *November 2012*		*7.6*	*7.8*	*7.9*
India	5.6	5.1	5.8	6.5
– *November 2012*		*5.5*	*6.2*	*6.9*

(1) In 2011.
(2) Based on purchasing power parity.
Sources: IHS Global Insight, International Monetary Fund, Datastream and Ministère des Finances et de l'Économie du Québec.

In the **euro area**, while financial markets have enjoyed a period of calm, the recession is expected to continue in 2013. Economic activity will recover only very gradually. Ongoing budget consolidation and the restrictive effects on credit stemming from the banks' financial situation, together with record-high unemployment rates in some countries, will continue to weigh on the region's growth outlook.

Nonetheless, the economic and financial situation should gradually stabilize. Accordingly, following a decline of 0.6% in 2012, real GDP in euro area should again contract in 2013, by 0.4%, followed by a gain of 0.5% in 2014.

In the **United Kingdom,** real GDP growth was 0.2% in 2012 and is expected to be 0.9% in 2013 and 1.3% in 2014. British economic growth remains limited by the austerity measures put in place to restore order to public finances and by the euro area's difficulties. Starting with the second half of 2013, the improving outlook for global growth should contribute to firmer economic growth in the United Kingdom.

Real GDP in **Japan**, after increasing by 2.0% in 2012, is expected to rise by 1.1% in 2013 and 1.2% in 2014. Japan entered into recession in the second quarter of 2012, with Japanese exports slowed by the impact of the euro area's economic difficulties and softer Chinese demand for Japanese products.

These difficulties have prompted the new Japanese government to adopt an ambitious stimulus plan and pressure the Bank of Japan to further ease monetary policy. The impact of these measures on domestic demand and the recovery in exports, helped by a weaker yen, should enable the Japanese economy to return to growth in 2013.

In **China**, economic activity should grow by 8.0% in 2013 and 7.8% in 2014, following a gain of 7.8% in 2012. In the short term, economic activity will continue to be affected by the recession in the euro area, the slow recovery in the United States and the slowdown in trade with Japan, three of its largest export markets. However, the measures taken by Chinese authorities will stimulate domestic demand. In addition, in the second half of 2013 and in 2014, China's economy will benefit from the improving economic situation in the euro area and the United States.

India's economy should grow by 5.1% in 2012, 5.8% in 2013 and 6.5% in 2014. The economy suffers from a low level of investment, sluggish world trade and high inflation that limits the central bank's leeway to stimulate the economy. However, the government has taken a number of important measures to stimulate growth and other economic reforms could be introduced.

3.4 Risks related to the economic forecast

This economic scenario is subject to several risks that could influence Québec's economic growth. Many of these risks were mentioned in the last budget and still apply. However, on the whole, risks have slightly abated since November 2012.

❑ Resurgence of the debt crisis in the euro area

European authorities adopted significant support measures for governments in difficulty in the summer and fall of 2012 that have reduced the risk of a breakup of the euro area in the short term.

However, euro area governments and banks remain fragile and the economic and budgetary adjustments necessary for the monetary union to operate smoothly in the long term are not over. The unemployment rate, which has hit record levels in some countries, is a particular risk for economic growth and political stability.

— A less favourable change in the euro area situation could lead to a resurgence in financial tensions. Among other things, this could limit access to financial markets for countries in difficulty and further reduce confidence of economic agents.

— More recently, the difficult financial situation of Cyprus has revived concerns and financial market tensions.

❑ Uncertain impact of fiscal and budgetary consolidation measures in the United States

Many measures aimed at reducing the U.S. budget deficit have been adopted and took effect in the first quarter of 2013.

— The agreement on the fiscal cliff reached in January 2013 includes tax increases for households that total over US$170 billion for 2013, i.e. 1.1% of GDP.

— The sequester that took effect on March 1, 2013 will reduce spending by more than US$65 billion in 2013, i.e. 0.4% of GDP. This is in addition to other budgetary restriction measures adopted in 2011.

The economic impact of these recent decisions could differ from what is expected.

— As experience and recent economic literature show, the impact of fiscal and budgetary consolidation measures is often under-estimated.

Accordingly, U.S. economic growth may have to be revised downward if the negative impact of budgetary restriction measures on the real economy turns out to be greater than forecast.

Conversely, the U.S. economy growth could be stronger than expected if improvements in economic fundamentals and consumer and business confidence mitigate the impact of austerity measures more than anticipated.

— In particular, the U.S. economy is benefiting from the recovery in the housing market, the acceleration in oil and gas production and the recent strength of the manufacturing sector.

— In addition, the measures adopted in early 2013 have helped to partially reduce uncertainty regarding budgetary and fiscal policy, which could lead to improved confidence among economic agents.

❑ Heightened geopolitical tensions

The current international situation is plagued by major persistent tensions in certain parts of the world that could threaten the global geopolitical balance.

Escalating geopolitical tensions could have negative consequences on global economic growth and generate significant unforeseen movements on financial markets.

— Growing uncertainty could in particular result in lower world trade and declining confidence among economic agents.

— In cases where an exacerbation in tensions would affect oil-producing countries, a sudden rise in the price of oil would slow world economic growth.

4. THE MAIN METALS PRODUCED IN QUÉBEC

Québec has abundant mineral resources. Although, because of Québec's highly diversified economy, the mining sector is still relatively small in terms of its share of GDP, it makes an important contribution to the development of the economy. Mineral extraction has a ripple effect on related industries, in particular primary metal processing, construction and transportation, thus contributing to job creation.

— In 2011, the contribution of the mining sector, including mining extraction, oil and gas as well as support activities, accounted for 1.2% of Québec's economic activity.

— Mining sector investment amounted to $3.9 billion in 2011 and $4.8 billion in 2012, a record high. According to a survey in March 2013 by the Institut de la statistique du Québec, investment intentions for 2013 remain high, at $4.1 billion, indicative of the sector's positive outlook in Québec.

— Almost 17 000 jobs were tied to mining extraction as well as smelting, refining and processing in Québec in 2011.

  — Many thousands of other jobs are indirectly tied to the mining industry, whether through investments in new mining projects or existing projects, or in the transportation of metals and ore.

In addition, mining activities make a significant contribution to the development of the regions, with production and employment concentrated in the regions of Abitibi-Témiscamingue, Côte-Nord and Nord-du-Québec.

The prices of metals produced in Québec, in particular iron, gold, nickel and zinc, are set on international markets. Accordingly, the mining industry is subject to global economic cycles.

— The prices of metals produced in Québec have fluctuated over the past year because of uncertainties regarding the world economy.

— Despite these cyclical variations, metal prices should remain relatively high because of strong demand from emerging economies.

This section gives an overview of the market outlook for the main metals produced in Québec.

— Iron, gold and nickel are Québec's three largest mineral productions, accounting for almost 60% of the total in 2012.

Québec metal price index[1]

The difficult international situation is reflected in the prices of metals produced in Québec

In 2012, prices of metals produced in Québec fell 11% compared to the previous year, on the heels of a deceleration in global economic activity.

- The recession in Europe, as well as slowing growth in emerging countries, dampened global demand for metals.

Accordingly, the Québec metal price index fell 22%, from 242 points in August 2011 to 189 points in August 2012. It then recovered to 212 points in February 2013, a gain of 12%.

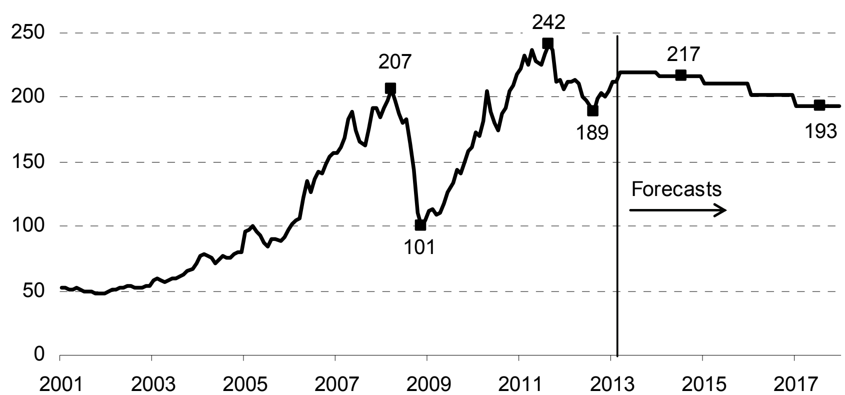
Prices for natural resources have fluctuated significantly. Despite recent declines, prices for metals produced in Québec remain relatively high compared to the lows reached during the last recession and to levels observed in the early 2000s.

Outlook for metal prices

In 2013 and 2014, the Québec metal price index should remain at levels similar to those of 2012, i.e. around 218 points on average.

- On the medium term, prices for nickel and zinc should rise, while the prices of iron ore and copper are expected to decline. The price of gold is expected to keep up in the short term and fall thereafter.
- Globally, the improvements in emerging economies will support global demand over the coming years, which will continue to foster investment in Québec's mining sector.

Québec metal price index
(U.S. dollars, March 2005 = 100)



Sources: Bloomberg, Natural Resources Canada, Institut de la statistique du Québec and Ministère des Finances et de l'Économie du Québec.

1 More detailed information on the composition of the index is available on page B.15 of the *Budget Plan 2013-2014*.

❑ Sharp rise in the supply of iron ore

In early 2012, the price of iron ore remained relatively stable. However, the iron ore market experienced turbulence in the second half of 2012.

— Following an important drop in the price of iron in the fall of 2012, accelerating growth in China and a wave of optimism on markets pushed the price of iron ore upward late in the year.

As to the outlook for iron ore prices, demand growth should remain sufficient for the current value to hold at around US$110 per tonne in the short term.

Thereafter, the price of iron ore should decline because of additional production from mining projects under development, which are expected to become operational over the coming years.

— In the medium term, the value or iron ore should decline to roughly US$95 per tonne. Nonetheless, this remains above prices that prevailed before 2007.

CHART A.49

Price of iron ore

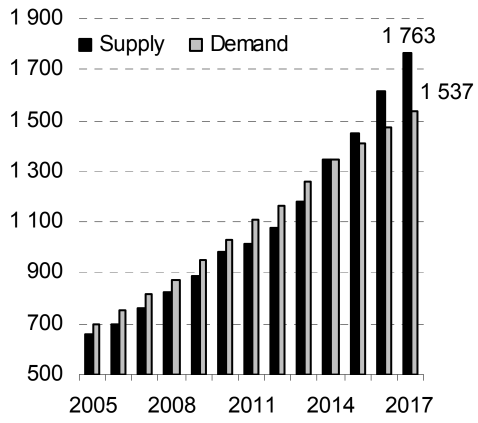
(US$ per tonne)

Source: Bloomberg.

CHART A.50

World supply of and demand for iron(1)

(millions of tonnes)



(1) On the seaborne market.
Source: Morgan Stanley.

❑ Global economic and financial uncertainties support the price of gold

Over the last two years, demand for gold from central banks has been remarkably high. This demand, combined with gold's investment allure, has supported high prices for the metal.

— Over the last five quarters, the value of gold has fluctuated within a bracket from US$1 560 to US$1 790 per ounce.

In the short term, the gold price should remain above US$1 500 per ounce.

— Continued quantitative easing as well as uncertainties regarding the global economic and financial situation should support the price of gold, which acts as a safe haven asset.

Subsequently, however, investment demand for gold should remain stable, while demand from central banks should gradually revert to being marginal as the global economic situation improves.

— These factors should cause the value of gold to decline, despite growing demand for industrial uses.

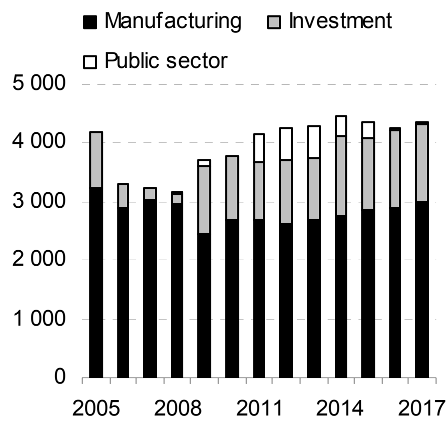
CHART A.51

Gold price
(U.S. dollars per ounce)

Source: Bloomberg.

CHART A.52

World demand for gold
(tonnes)



Source: Morgan Stanley.

❑ Positive outlook for nickel

After soaring and then plunging a few years ago, the price of nickel has reflected recently a more balanced relation between supply and demand.

— The price per tonne of nickel was close to US$17 000 at the end of 2012.

In the short term, the current high inventories will help contain price increases.

— Following a drop in 2010 and 2011, nickel inventories rose in 2012, ending the year at a very high level.

— Upward pressure on the price should increase once nickel inventories have declined.

Accordingly, the price of nickel should experience a rise in the long term, since growth in demand should exceed that of supply for an extended period.

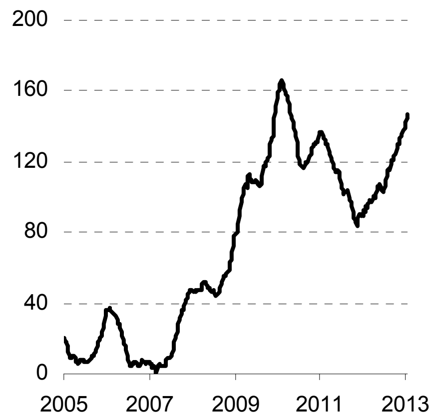
CHART A.53

Price of nickel
(US$ per tonne)

Source: Bloomberg.

CHART A.54

Nickel inventories
(millions of tonnes, London Metal Exchange)



Source: Bloomberg.

❑ The price of zinc supported by high inventories

In recent years, the price of zinc has ranged from US$1 700 to US$2 600 per tonne, substantially less than the US$4 500 per tonne reached in 2006.

After having been almost completely depleted in 2007, zinc inventories have since then risen strongly and currently stand at high levels. This increase has dampened price pressure, with supply rising at a pace comparable to demand.

— Over the past year, the price of zinc has remained stable, ranging between US$1 800 and US$2 200 per tonne.

The zinc market seems relatively balanced for 2013, but the closing in the near future or decline in production of certain major mines should propel prices higher over the coming years.

— The price of zinc is accordingly expected to reach roughly US$2 500 per tonne in the medium term.

Longer term, growth in demand should keep pace with that of supply, allowing the price to stabilize around this level.

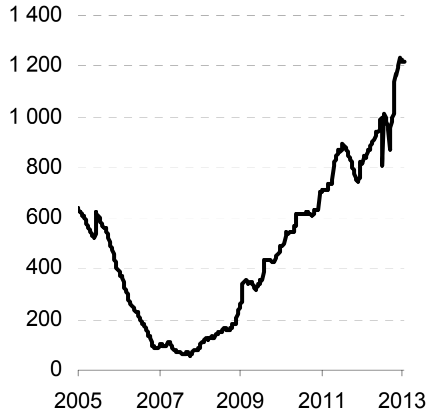
CHART A.55

Price of zinc
(US$ per tonne)

Source: Bloomberg.

CHART A.56

Inventories of zinc
(millions of tonnes, London Metal Exchange)



Source: Bloomberg.

❑ The price of copper will depend on Chinese demand

The price of copper has been less affected than most other industrial metals by the slowdown in the Chinese economy in 2012 and the continuing difficulties in advanced economies. In early 2013, it was roughly US$8 000 per tonne.

The short-term outlook for the copper market is positive. A wave of construction projects is underway in China and is currently at a stage that requires more copper.

— Chinese demand amounts to 40% of world consumption of copper.

In addition, continued economic growth at a steady pace in China will lead to sustained demand for household appliances and machinery and equipment, which is positive for the copper market.

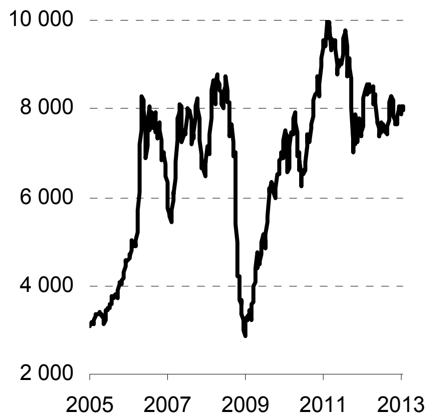
— Consequently, the price of copper is expected to remain relatively high, around US$8 000 per tonne over the next two years.

In the longer term, significant growth in supply and a slowing pace of new residential construction in China should lead to a decline in the price of copper.

— Copper is accordingly expected to trade at roughly US$7 000 per tonne in the medium term.

CHART A.57

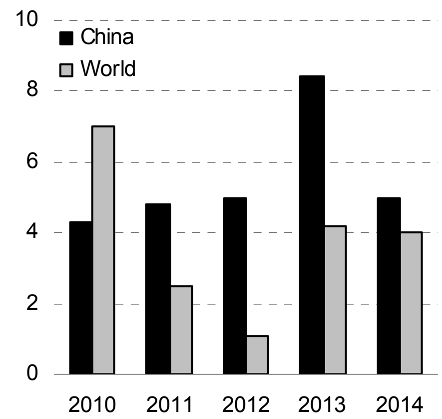
Price of copper
(US$ per tonne)



Source: Bloomberg.

CHART A.58

Demand for copper
(percentage growth)



Source: Morgan Stanley.

Section B

THE GOVERNMENT'S FINANCIAL SITUATION

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INTRODUCTION

This section of the March 2013 *Update on Québec's Economic and Financial Situation* presents the changes in the financial framework since the 2013-2014 Budget was tabled in November 2012.[1]

The information provided in this respect focuses on changes in the financial situation, namely:

— adjustments to the financial framework since the November 2012 Budget;

— consolidated expenditure;

— the government's financial framework, i.e. forecasts until 2017-2018;

— public capital investment.

1 In this section, the budget data for 2012-2013 are preliminary and data for 2013-2014 and subsequent years are forecasts.

1. THE GOVERNMENT'S FINANCIAL SITUATION

1.1 The budgetary objectives in Budget 2013-2014 are maintained

The government is maintaining the budgetary objectives set in Budget 2013-2014 bearing in mind recent changes in the economic outlook.

Accordingly, the government is confirming:

— the maintenance, for 2012-2013, of the budget deficit target of $1.5 billion as anticipated last November, excluding the accounting impact stemming from Hydro-Québec's exceptional loss for the closure of the Gentilly-2 nuclear power plant;

— the return to fiscal balance in 2013-2014 and maintenance of such balance in subsequent years, in accordance with the *Balanced Budget Act.*

These objectives will be attained while payments to the Generations Fund will be maintained.

Moreover, the impact for 2012-2013 of the exceptional loss from the closure of the Gentilly-2 nuclear power plant, recorded in Hydro-Québec's financial statements as at December 31, 2012, now stands at $1 876 million, as against $1 805 million as at November 20, 2012.

TABLE B.1

Return to fiscal balance – March 2013
(millions of dollars)

	2012-2013	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
SURPLUS (DEFICIT)	**–2 440**	**1 053**	**1 368**	**1 876**	**2 165**	**2 655**
Payments of revenue dedicated to the Generations Fund	–936	–1 053	–1 368	–1 876	–2 165	–2 655
Exclusion of the exceptional loss – Closure of Gentilly-2(1)	1 876	—	—	—	—	—
BUDGETARY BALANCE(2)	**–1 500**	**—**	**—**	**—**	**—**	**—**

(1) For 2012-2013, the budgetary balance excludes the accounting impact stemming from Hydro-Québec's exceptional loss for the closure of the Gentilly-2 nuclear power plant. The impact stands at $1 876 million, i.e. $71 million more than the $1 805 million estimated in Budget 2013-2014.
(2) Budgetary balance within the meaning of the *Balanced Budget Act.*

1.1.1 The government's financial framework

The following table presents the government's financial framework from 2012-2013 to 2014-2015.

For 2012-2013, budgetary revenue stands at $68.7 billion and budgetary expenditure totals $70.5 billion.

— Bearing in mind the results of the consolidated entities and the maintenance of a $50-million contingency reserve, the budget deficit stands at $1.5 billion, equivalent to 0.4% of GDP.

Fiscal balance will be achieved, as anticipated, in 2013-2014. Budgetary revenue and expenditure will stand at $72.1 billion and $72.3 billion, respectively. A $200-million contingency reserve is being maintained for this year.

For 2014-2015, balance is maintained, with budgetary revenue of $74.1 billion and budgetary expenditure of $73.9 billion. A $300-million contingency reserve is being maintained for that year. Moreover, as indicated last November, the financial framework indicates a shortfall of $430 million to be offset as of 2014-2015.

TABLE B.2

Summary of adjusted budgetary transactions – March 2013
(millions of dollars)

	2012-2013	2013-2014	2014-2015
BUDGETARY TRANSACTIONS			
Budgetary revenue	68 652	72 109	74 133
% change	*4.8*	*5.0*	*2.8*
Budgetary expenditure	–70 464	–72 341	–73 946
% change	*2.3*	*2.7*	*2.2*
Consolidated entities	1 298	1 485	1 051
Contingency reserve	–50	–200	–300
Shortfall to be offset	—	—	430
Exceptional loss – Closure of Gentilly-2	–1 876	—	—
SURPLUS (DEFICIT)	**–2 440**	**1 053**	**1 368**
BALANCED BUDGET ACT			
Payments of revenue dedicated to the Generations Fund	–936	–1 053	–1 368
Exclusion – Exceptional loss	1 876	—	—
BUDGETARY BALANCE(1)	**–1 500**	**—**	**—**
As a % of GDP	***–0.4***	**—**	**—**

(1) Budgetary balance within the meaning of the *Balanced Budget Act.*

1.2 Summary of adjustments from 2012-2013 to 2014-2015

The government is maintaining the budgetary objectives set in Budget 2013-2014 despite more moderate economic growth.

The update to the financial framework reflects the recent change to the government's revenue and to the economic outlook for 2013 and 2014. Own-source revenue is adjusted downward by $250 million in 2012-2013 and $565 million in 2013-2014.

These adjustments stem in particular from:

— the lower yield from the QST resulting from weaker consumption than expected in the second half of 2012;

— lower revenue from corporate taxes attributable, in particular, to a less favourable international situation.

However, these adjustments are completely offset by:

— a reduction debt service because of lower interest rates than forecast;

— an unexpected increase in equalization payments further to updated economic and fiscal data;

— use of part of the contingency reserves incorporated in the November 2012 financial framework.

These changes make it possible to maintain the budgetary objectives set last November as they stand.

Moreover, the financial framework reflects the decisions made following the Sommet sur l'enseignement supérieur, held last February 25 and 26, concerning student financial assistance in particular.

— The improvements to student financial assistance result in a $34-million increase in program spending in 2013-2014 and a $61-million increase in 2014-2015, in particular for the gradual rise to $45 000 of the parents' income threshold beyond which their income is considered in the calculation of student assistance. These measures will be funded by reducing the rate of the tax credit for tuition fees and examination fees from 20% to 8%.

TABLE B.3

Financial framework – Adjustments to Budget 2013-2014

(millions of dollars)

	2012-2013	2013-2014	2014-2015
BUDGETARY BALANCE – NOVEMBER 2012[1]	**–1 500**	—	—
Adjustments related to the economic outlook			
Own-source revenue[2]	–250	–565	–575
Federal transfers	5	280	175
Debt service	95	85	200
	–150	**–200**	**–200**
Other adjustments			
Sommet sur l'enseignement supérieur			
Reduction from 20% to 8% in the rate of the tax credit for tuition and examination fees	—	34	61
Additional spending stemming from the improvement to the student financial assistance program[3]	—	–34	–61
Use of contingency reserves	150	200	200
	150	**200**	**200**
Total adjustments	**—**	**—**	**—**
BUDGETARY BALANCE – MARCH 2013[1]	**–1 500**	**—**	**—**
As a % of GDP	***-0.4***	**—**	**—**

(1) Budgetary balance within the meaning of the *Balanced Budget Act.*
(2) Excludes savings stemming from the adjustment of tax assistance for students.
(3) For details of the enhancement of the student financial assistance program, see section D, "Implementation of the Economic Vision."

❑ Attainment in 2012-2013 of the $1.5-billion budget deficit target

For 2012-2013, the $250-million downward adjustment in own-source revenue stemming from the greater than anticipated economic slowdown in 2012 was offset, in particular, by:

- a $95-million downward adjustment in debt service;
- the use of a portion of the contingency reserve, i.e. $150 million.

Accordingly, a $50-million reserve has been maintained in the financial framework at the end of the government's fiscal year.

❑ Attainment in 2013-2014 of fiscal balance

For 2013-2014, which marks the return to fiscal balance, the $565-million downward adjustment in own-source revenue is offset by:

- a $280-million upward adjustment in federal transfers, mainly because of an increase in equalization revenue;
- an $85-million downward adjustment in debt service;
- a reduction from $400 million to $200 million in the contingency reserve.

❑ Maintenance of fiscal balance for 2014-2015

The $575-million downward adjustment in own-source revenue for 2014-2015 is entirely offset by:

- a $175-million upward adjustment in federal transfers;
- a $200-million downward adjustment in debt service;
- a reduction from $500 million to $300 million in the contingency reserve.

Moreover, as indicated in Budget 2013-2014, the financial framework indicates a shortfall of $430 million to be offset as of 2014-2015.

❑ Contingency reserves

The financial framework presented in the November 2012 budget included contingency reserves of $200 million in 2012-2013, $400 million in 2013-2014 and $500 million as of 2014-2015 in order, notably, to anticipate certain adjustments attributable to economic uncertainty.

To offset the adjustments related to the economic outlook, the government is using a portion of the contingency reserves:

— $150 million in 2012-2013;

— $200 million in 2013-2014 and 2014-2015.

Accordingly, the financial framework now includes, for each of these years, contingency reserves of $50 million, $200 million and $300 million.

TABLE B.4

Contingency reserves included in the financial framework – Adjustments to Budget 2013-2014
(millions of dollars)

	2012-2013	2013-2014	2014-2015
November 2012	200	400	500
Adjustments	–150	–200	–200
MARCH 2013	**50**	**200**	**300**

1.3 Detailed adjustments in 2012-2013 and 2013-2014

This section presents the detailed adjustments to budgetary revenue and budgetary expenditure for 2012-2013 and 2013-2014 in relation to November 2012.

TABLE B.5

Financial framework for 2012-2013 and 2013-2014 – Detailed adjustments to Budget 2013-2014
(millions of dollars)

	2012-2013			2013-2014		
	November 2012	**Adjust-ments**	**March 2013**	**November 2012**	**Adjust-ments**	**March 2013**
Own-source revenue						
Personal income tax	19 368	–125	19 243	20 365	–101	20 264
Contributions to the Health Services Fund	6 507	35	6 542	6 752	–35	6 717
Consumption taxes	16 210	–135	16 075	17 231	–183	17 048
Corporate taxes	4 209	–65	4 144	4 652	–138	4 514
Natural resources	233	–35	198	300	–62	238
Government enterprises	4 920	65	4 985	5 108	—	5 108
Other	1 745	10	1 755	1 807	–12	1 795
Subtotal	**53 192**	**–250**	**52 942**	**56 215**	**–531**	**55 684**
Federal transfers	15 705	5	15 710	16 145	280	16 425
Total budgetary revenue	**68 897**	**–245**	**68 652**	**72 360**	**–251**	**72 109**
Program spending	–62 642	—	–62 642	–63 791	–34	–63 825
Debt service	–7 917	95	–7 822	–8 601	85	–8 516
Total budgetary expenditure	**–70 559**	**95**	**–70 464**	**–72 392**	**51**	**–72 341**
Net results of consolidated entities	**1 241**	**57**	**1 298**	**1 471**	**14**	**1 485**
Contingency reserves	–200	150	–50	–400	200	–200
Exceptional loss – Closure of Gentilly-2	–1 805	–71	–1 876	—	—	—
SURPLUS (DEFICIT)	**–2 426**	**–14**	**–2 440**	**1 039**	**14**	**1 053**
BALANCED BUDGET ACT						
Payments of revenue dedicated to the Generations Fund	–879	–57	–936	–1 039	–14	–1 053
Exclusion – Exceptional loss	1 805	71	1 876	—	—	—
BUDGETARY BALANCE[1]	**–1 500**	**—**	**–1 500**	**—**	**—**	**—**

Note: In the case of adjustments, a minus sign indicates a reduction in revenue or an increase in expenditure.
(1) Budgetary balance within the meaning of the *Balanced Budget Act*.

1.3.1 Adjustments to budgetary revenue

❑ Own-source revenue

Own-source revenue mainly comprises tax revenues, i.e. personal income tax, contributions to the Health Services Fund, corporate taxes and consumption taxes. Changes in such revenues are closely linked to economic activity and to changes in taxation systems.

Own-source revenue also includes revenue from government enterprises and administrative revenue such as duties and licenses, interest and fines.

■ 2012-2013 and 2013-2014

For the 2012-2013 fiscal year, own-source revenue stands at over $52.9 billion, up 5.3% over 2011-2012. For fiscal year 2013-2014, own-source revenue will rise by 5.2%, to $55.7 billion.

Own-source revenue has been adjusted downward by $250 million in 2012-2013 and $531 million in 2013-2014[2] in relation to what was anticipated in Budget 2013-2014, mainly because of:

— downward adjustments of $125 million in 2012-2013 and $101 million in 2013-2014 in revenue from personal income tax, attributable, in particular, to lower than anticipated tax instalments in 2012 paid by self-employed workers, the impact of which will continue to be felt in 2013;

— reductions of $135 million in 2012-2013 and $183 million in 2013-2014 in consumption tax revenue, which reflects, in particular, lower retail sales;

— downward adjustments of $65 million and $138 million, for 2012-2013 and 2013-2014, respectively, in corporate tax revenue, a reflection a lower than anticipated growth in corporate profits for 2012 and 2013;

— reductions of $35 million in 2012-2013 and $62 million in 2013-2014 in natural resource revenue, attributable to a decrease in the value of mining production subject to mining duties;

— for 2012-2013 only, revenue from government enterprises has been adjusted upward by $65 million.

2 Includes the savings arising from the adjustment to student financial assistance.

❑ Impact of the decision of the Régie de l'énergie

■ Incentive regulation mechanism and transition measure announced in Budget 2013-2014

In the last budget, the government announced the possible implementation of an incentive regulation mechanism by the Régie de l'énergie to allow consumers and Hydro-Québec to share efficiency gains.

Until then, the government has put forward a transition measure that sets the operating expenses of Hydro-Québec's regulated divisions for 2013-2014. For the government corporation, the anticipated and achieved efficiency gains of $225 million will lead, in particular, to a staff reduction of 2 000, through attrition, by the end of 2013.

■ Maintenance of Hydro-Québec's net earnings for 2013-2014

On March 13, 2013, the Régie de l'énergie handed down its decision in the Hydro-Québec Distribution rate case and granted it a 2.4% rate increase regardless of the operating expenses set in the last budget. Accordingly, in relation to the 3.4% increase requested by Hydro-Québec, this represents a reduction on the order of $100 million on anticipated net earnings. Hydro-Québec will have to generate revenue to offset the shortfall.

Accordingly, Hydro-Québec will achieve the anticipated net earnings of $2 725 million for 2013-2014.

TABLE B.6

Adjustment to Hydro-Québec's net earnings
(millions de dollars)

	2013-2014
Required revenue (mainly from electricity rates)	
Requested from the Régie de l'énergie by Hydro-Québec	–11 100
Granted by the Régie de l'énergie in March 2013	11 000
Impact of the decision by the Régie de l'énergie	**–100**
Additional revenue to be generated by Hydro-Québec	100
Adjustment to Hydro-Québec's net earnings	**—**

❑ Federal transfer revenues

In relation to the November 2012 budget, federal transfer revenues have been adjusted upward by $5 million in 2012-2013 and $280 million in 2013-2014.

For 2012-2013, the adjustment stems from a $30-million increase in health transfers and a $7-million increase in transfers for postsecondary education and other social programs, attributable, essentially, to a reduction in the value of the special Québec abatement, which is deducted from the transfers. The increases are offset by a $32-million downward adjustment in other programs, mainly attributable to a downward adjustment in the compensatory payment concerning the Canada Student Loans Program that Québec receives in exchange for its right of withdrawal from the federal program.

For 2013-2014, the adjustment stems primarily from a $255-million upward adjustment in equalization payments announced by the federal government in December 2012[3] in relation to what was anticipated in the November 2012 budget. This positive adjustment has resulted, among other things, from the improvement in Ontario's economic position, which has increased its relative fiscal capacity, thereby leading to equalization gains for the other recipient provinces.

— From 2009-2010 to 2011-2012, Ontario's share of the corporate tax base rose significantly. In the context of equalization, this relative improvement benefits the other recipient provinces, including Québec.

TABLE B.7

Federal transfer revenues – Adjustments to Budget 2013-2014
(millions of dollars)

	2012-2013	2013-2014
NOVEMBER 2012	**15 705**	**16 145**
% change	***3.0***	***2.8***
Equalization	—	255
Health transfers	30	22
Transfers for post-secondary education and other social programs	7	6
Other programs	–32	–3
Total adjustments	**5**	**280**
MARCH 2013	**15 710**	**16 425**
% change	***3.1***	***4.6***

3 In December 2012, under the renewal of federal transfers for 2014, the federal government announced technical changes that will be applied to the equalization program as of 2014-2015, until 2018-2019. The changes will have a positive impact of roughly $40 million a year on Québec's federal transfer revenue.

1.3.2 Adjustments to budgetary expenditure

Budgetary expenditure, which includes program spending and debt service, has been adjusted downward by $95 million in 2012-2013 and $51 million in 2013-2014.

❑ Program spending

The program spending target for 2012-2013 is being maintained at $62 642 million, up 1.9% in relation to the real results for 2011-2012.

— The government has taken the necessary steps to offset the significant overruns noted in September 2012 and maintain the 2012-2013 program spending objective set in March 2012.

For 2013-2014, the program spending objective is being increased by $34 million in relation to the target set in the last budget, to $63 825 million, a 1.9% increase. This increase stems solely from enhancements to student financial assistance agreed upon at the Sommet sur l'enseignement supérieur last February. The additional expenditure will be financed through savings in tax assistance for students resulting from the reduction from 20% to 8% in the rate of the tax credit for tuition and examination fees.

With the exception of the impact of enhancements to student financial assistance, no adjustments in program spending are being made in 2014-2015. Accordingly, the program spending objective stands at $65 411 million, i.e. a 2.5% increase in relation to 2013-2014.

TABLE B.8

Program spending – Adjustments to Budget 2013-2014
(millions of dollars)

	2012-2013	2013-2014	2014-2015
NOVEMBER 2012	**62 642**	**63 791**	**65 350**
% change	***1.9***	***1.8***	***2.4***
Additional expenditure stemming from the enhancement of the student financial assistance program(1)	—	34	61
MARCH 2013	**62 642**	**63 825**	**65 411**
% change	***1.9***	***1.9***	***2.5***

(1) For details of the enhancement of the student financial assistance program, see section D, "Implementation of the Economic Vision."

■ Changes in program spending

Average program spending growth from 2012-2013 to 2014-2015 stands at 2.1%, significantly lower than the 5.6% average growth observed between 2006-2007 and 2009-2010, and that observed in 2010-2011 and 2011-2012. More specifically, program spending should increase by:

— 1.9% in 2012-2013;

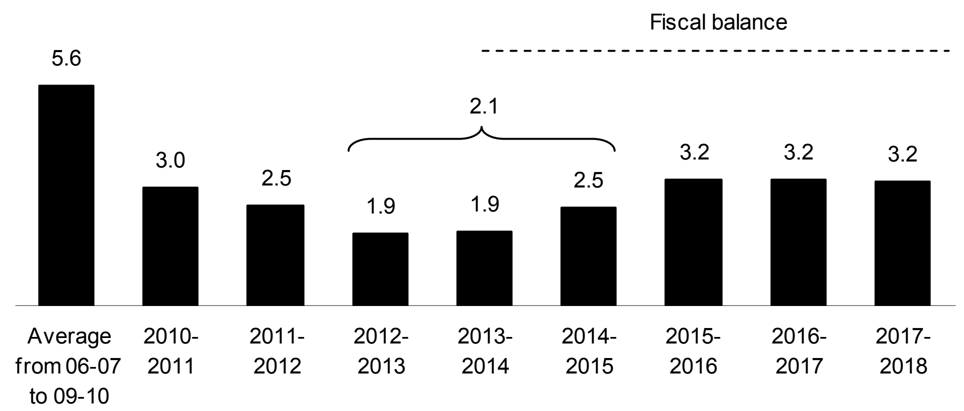
— 1.9% in 2013-2014;

— 2.5% in 2014-2015.

As of 2015-2016, program spending will keep pace with revenue, thereby ensuring that fiscal balance is maintained.

CHART B.1

Program spending growth
(per cent)



❑ Debt service

For 2012-2013, the debt service of the general fund is $95 million lower than what was forecast in the November 2012 budget, mainly because of lower than anticipated long-term interest rates.

For 2013-2014, debt service has been adjusted downward by $85 million in relation to the forecast in the November 2012 budget. This adjustment is attributable, by and large, to higher than anticipated revenue from the Retirement Plans Sinking Fund (RPSF). Revenue from the RPSF is recorded as a deduction from debt service.

TABLE B.9

Debt service of the general fund – Adjustments to Budget 2013-2014
(millions of dollars)

	2012-2013			2013-2014		
	November 2012	Adjustments	March 2013	November 2012	Adjustments	March 2013
Direct debt service	4 928	–85	4 843	5 335	45	5 380
Retirement plan interest costs(1)	3 008	–10	2 998	3 287	–130	3 157
Employee future benefits interest costs(2)	–19	—	–19	–21	—	–21
DEBT SERVICE OF THE GENERAL FUND	**7 917**	**–95**	**7 822**	**8 601**	**–85**	**8 516**

(1) Corresponds to the interest on the obligation respecting the retirement plans of public and parapublic sector employees reduced by investment income of the Retirement Plans Sinking Fund.
(2) Corresponds to the interest on the obligation respecting the Survivor's Pension Plan reduced by investment revenue from the Survivor's Pension Plan Fund and interest on the obligation in respect of accumulated sick leave reduced by investment income of the Accumulated Sick Leave Fund.

1.3.3 The government's consolidated expenditure

The following table indicates the level of and changes in the components of consolidated expenditure, i.e. all public expenditures included in the government's reporting entity.

- In addition to program spending, consolidated expenditure includes, in particular, that of the special funds, non-budget-funded bodies, establishments in the health and social services and the education networks, and debt service.

- Growth in consolidated expenditure, excluding debt service, will average 2.7% from 2012-2013 to 2014-2015.

TABLE B.10

Consolidated expenditure – March 2013

(millions of dollars)

	2012-2013	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
Expenditure						
General fund	62 642	63 825	65 411	67 502	69 665	71 881
% change	*1.9*	*1.9*	*2.5*	*3.2*	*3.2*	*3.2*
Special funds	7 521	8 270	8 520	8 782	8 957	9 175
% change	*14.4*	*10.0*	*3.0*	*3.1*	*2.0*	*2.4*
Non-budget-funded bodies	17 547	18 334	19 084	20 303	21 042	21 750
% change	*5.1*	*4.5*	*4.1*	*6.4*	*3.6*	*3.4*
Health and social services and education networks	35 883	36 842	37 908	38 898	40 304	41 677
Specified purpose accounts	1 173	1 077	1 161	958	958	958
Expenditure funded by the taxation system(1)	6 174	6 202	6 282	6 398	6 489	6 488
Consolidation adjustments(2)	–49 979	–51 516	–53 212	–55 423	–57 577	–59 558
Consolidated expenditure excluding debt service	**80 961**	**83 034**	**85 154**	**87 418**	**89 838**	**92 371**
% change	***2.8***	***2.6***	***2.6***	***2.7***	***2.8***	***2.8***
Debt service						
General fund	7 822	8 516	8 535	8 652	8 749	8 934
Consolidated entities(3)	2 125	2 251	2 449	2 788	3 102	3 498
Consolidated debt service	**9 947**	**10 767**	**10 984**	**11 440**	**11 851**	**12 432**
% change	***5.2***	***8.2***	***2.0***	***4.2***	***3.6***	***4.9***
CONSOLIDATED EXPENDITURE	**90 908**	**93 801**	**96 138**	**98 858**	**101 689**	**104 803**

(1) Doubtful tax accounts are included.
(2) The consolidation adjustments stem mainly from the elimination of reciprocal transactions between entities in different sectors.
(3) Includes consolidation adjustments.

❑ Change in consolidated expenditure excluding debt service

On the whole, growth in consolidated expenditure excluding debt service will stand, on average, at 2.7% between 2012-2013 and 2014-2015, lower than the 5.7% growth observed for the period 2006-2007 to 2009-2010 and the growth observed in 2010-2011 and in 2011-2012.

More specifically, consolidated expenditure, excluding debt service, should increase by:

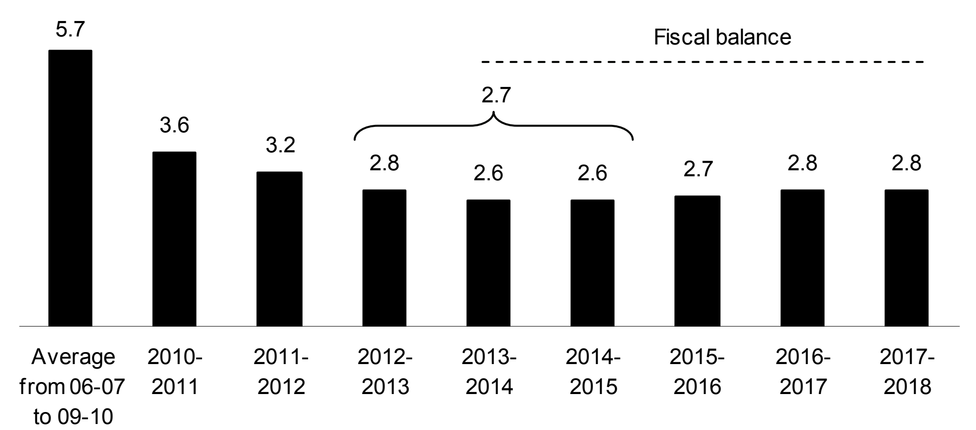
— 2.8% in 2012-2013;

— 2.6% in 2013-2014;

— 2.6% in 2014-2015.

CHART B.2

Growth in consolidated expenditure excluding debt service
(as a percentage)



Spending growth in some jurisdictions

Like Québec, several jurisdictions have had to adjust their financial framework because of lower than anticipated economic growth. Accordingly, from 2012 to 2014, a number of jurisdictions are having to rely on limited spending growth to attain their budgetary objectives.

- In Québec, consolidated expenditure excluding debt service will grow by 2.8% in 2012-2013, 2.6% in 2013-2014 and 2.6% in 2014-2015.

For the federal government and for the provinces that, to date, have tabled their 2013-2014 budget, some adjustments to spending growth have been made.

- The Alberta government anticipates a spending reduction of 1.2% in 2013-2014 and a 2.0% increase in 2014-2015.
- British Columbia is banking on spending growth limited to 0.6% and 0.9% for 2013-2014 and 2014-2015, respectively.
- The federal government anticipates spending growth of 0.8% in 2013-2014, down 2.1 percentage points in relation to 2012-2013.

Spending growth is also very limited at the international level.

Spending growth by jurisdiction – 2012 to 2014
(per cent)

	2012	2013	2014
Consolidated spending(1) – 2013-2014 budgets			
Québec – March 2013	**2.8**	**2.6**	**2.6**
Alberta	7.8	-1.2	2.0
British Columbia	3.5	0.6	0.9
Federal government	2.9	0.8	1.2
Consolidated spending(2)			
United States(3)	-1.6	0.4	0.9
United Kingdom	2.5	2.1	0.8
France	2.7	2.9	3.1
Italy	0.2	0.5	0.8
Euro area(4)	1.5	1.9	2.3

(1) Consolidated spending excluding debt service is presented by fiscal year for the provincial and federal governments only.
(2) Such spending represents current spending excluding debt service for all orders and levels of government, except for the United States.
(3) Includes the impact of the fiscal cliff for 2013 and 2014, i.e. the automatic spending cuts and tax increases.
(4) Spending growth for the 17 euro area countries.
Sources: 2013-2014 budgets of the provinces, the federal government and the United Kingdom, as well as the Congressional Budget Office and the European Commission (Écofin, winter 2013).

❑ Consolidated debt service

Consolidated debt service should rise by 5.2% in 2012-2013. The increase is mainly attributable to the increase in the debt and the impact of the yields of the Caisse de dépôt et placement du Québec on the income of the Retirement Plans Sinking Fund, which are recorded as a deduction against retirement plans interest costs.

In 2013-2014, the 8.2% growth in consolidated debt service stems from the anticipated increase in interest rates, the increase in the debt and the impact of the yields of the Caisse de dépôt et placement du Québec on the income of the Retirement Plans Sinking Fund.

In 2014-2015, a 2.0% increase is anticipated, primarily because of the anticipated increase in interest rates.

TABLE B.11

Consolidated debt service – March 2013
(millions of dollars)

	2012-2013	2013-2014	2014-2015
Direct debt service	4 843	5 380	5 583
Retirement plans interest costs(1)	2 998	3 157	2 979
Employee future benefits interest costs(2)	–19	–21	–27
Debt service of the general fund	**7 822**	**8 516**	**8 535**
% change	***6.5***	***8.9***	***0.2***
Debt service of consolidated entities	2 125	2 251	2 449
% change	*1.0.*	*5.9*	*8.8*
CONSOLIDATED DEBT SERVICE	**9 947**	**10 767**	**10 984**
% change	***5.2***	***8.2***	***2.0***

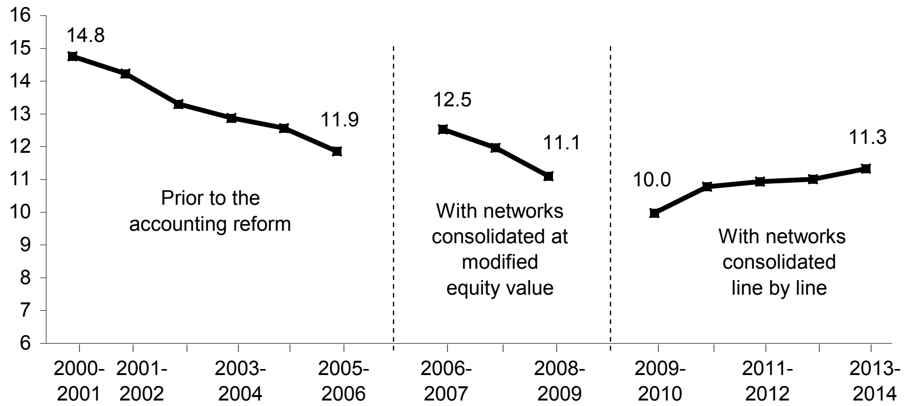
(1) Corresponds to the interest on the obligation respecting the retirement plans of public and parapublic sector employees reduced by investment income of the Retirement Plans Sinking Fund.
(2) Corresponds to the interest on the obligation respecting the Survivor's Pension Plan reduced by investment income from the Survivor's Pension Plan Fund and interest on the obligation in respect of accumulated sick leave reduced by investment income of the Accumulated Sick Leave Fund.

Share of revenue devoted to consolidated debt service

The share of revenue devoted to consolidated debt service should stand at 11.3% in 2013-2014, as against 14.8% in 2000-2001.

CHART B.3

Consolidated debt service
(as a percentage of consolidated revenue)



Efforts by consolidated entities

Reduction in expenditures of bodies and special funds

As is the case for all government departments, non-budget-funded bodies and special funds must contribute to the government's budgetary effort by reducing their spending growth.

Accordingly, the government announced in Budget 2013-2014 that the operating and remuneration expenditures of non-budget-funded bodies and special funds for 2013-2014 will be reduced, on average, by 2% or according to an amount determined by the government.

The budgetary yield of this cost-saving measure, established at $200 million for 2013-2014, is being maintained.

Work is under way to determine the amount of the spending reductions specific to each entity. Official targets will be conveyed at the beginning of the 2013-2014 fiscal year. The entities will also receive instructions specifying procedures governing accountability and follow-up in respect of the reductions.

Moreover, other government organizations engaged in fiduciary transactions that do not affect the government's consolidated results must also, for the sake of fairness, participate in the government's spending reduction efforts. The yield of such efforts will benefit the plans concerns and their trustees.

1.4 Detailed results

The following tables provide a detailed view of the major items that make up the government's financial framework.

TABLE B.12

Revenue of the general fund – March 2013
(millions of dollars)

	2012-2013	% change	2013-2014	% change
Own-source revenue				
Personal income tax	19 243	1.4	20 264	5.3
Contributions to the Health Services Fund	6 542	4.7	6 717	2.7
Consumption taxes	16 075	11.5	17 048	6.1
Corporate taxes	4 144	6.4	4 514	8.9
Revenue from government enterprises	4 985	5.0	5 108	2.5
Other revenue	1 953	-1.6	2 033	4.1
Total own-source revenue	**52 942**	**5.3**	**55 684**	**5.2**
Federal transfers				
Equalization	7 391	–5.4	7 833	6.0
Protection payment	362	—	—	—
Health transfers	4 792	6.2	5 140	7.3
Transfers for post-secondary education and other social programs	1 486	-0.1	1 545	4.0
Other programs	946	-10.8	870	-8.0
Harmonization of the QST with the GST – Compensation(1)	733	—	1 037	—
Total federal transfers	**15 710**	**3.1**	**16 425**	**4.6**
BUDGETARY REVENUE	**68 652**	**4.8**	**72 109**	**5.0**

(1) Bearing in mind the $430 million paid into the Fund to Finance Health and Social Services Institutions, the payment, for 2013-2014, totals $1 467 million.

TABLE B.13

Expenditure of the general fund – March 2013
(millions of dollars)

	2012-2013	% change	2013-2014	% change
Program spending	–62 642	1.9	–63 825	1.9
Debt service	–7 822	6.5	–8 516	8.9
BUDGETARY EXPENDITURE	**–70 464**	**2.3**	**–72 341**	**2.7**

1.5 The government's financial framework

1.5.1 The five-year financial framework

The government's financial framework confirms that fiscal balance will be restored in 2013-2014 and maintained thereafter, as stipulated in the *Balanced Budget Act.*

From 2012-2013 to 2014-2015, responsible spending management and revenue efforts will mean that annual growth in budgetary revenue outstrips growth in budgetary expenditure.

— Average annual growth in budgetary revenue will stand at 4.2% and that in budgetary expenditure will stand at 2.4%. This difference will allow the return to fiscal balance in 2013-2014.

Moreover, as indicated in Budget 2013-2014, the financial framework indicates a shortfall of $430 million to be offset as of 2014-2015.

As of 2015-2016, budgetary revenue and budgetary expenditure will grow at more or less the same pace, thereby ensuring that fiscal balance is maintained.

What is more, contingency reserves of $50 million in 2012-2013, $200 million in 2013-2014 and $300 million in 2014-2015 are included in the financial framework.

— As of 2015-2016, the contingency reserve stands at $400 million.

Moreover, the government is pursuing the debt-reduction objectives stipulated in the *Act to reduce the debt and establish the Generations Fund.*

For 2013-2014 and 2014-2015, payments of $1 053 million and $1 368 million will be made to the Generations Fund.

— In 2017-2018, the payments will reach $2 655 million.

TABLE B.14

Québec government's financial framework – March 2013
(millions of dollars)

	2012-2013	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
Budgetary revenue(1)						
Own-source revenue	52 942	55 684	58 066	60 052	62 096	64 021
% change	*5.3*	*5.2*	*4.3*	*3.4*	*3.4*	*3.1*
Federal transfers	15 710	16 425	16 067	16 448	16 853	17 239
% change	*3.1*	*4.6*	*-2.2*	*2.4*	*2.5*	*2.3*
Total budgetary revenue	**68 652**	**72 109**	**74 133**	**76 500**	**78 949**	**81 260**
% change	***4.8***	***5.0***	***2.8***	***3.2***	***3.2***	***2.9***
Budgetary expenditure(1)						
Program spending	–62 642	–63 825	–65 411	–67 502	–69 665	–71 881
% change	*1.9*	*1.9*	*2.5*	*3.2*	*3.2*	*3.2*
Debt service	–7 822	–8 516	–8 535	–8 652	–8 749	–8 934
% change	*6.5*	*8.9*	*0.2*	*1.4*	*1.1*	*2.1*
Total budgetary expenditure	**–70 464**	**–72 341**	**–73 946**	**–76 154**	**–78 414**	**–80 815**
% change	***2.3***	***2.7***	***2.2***	***3.0***	***3.0***	***3.1***
Consolidated entities						
Non-budget-funded bodies and special funds(2)	462	432	–317	–376	–565	–475
Health and social services and education networks	–100	—	—	—	—	—
Generations Fund	936	1 053	1 368	1 876	2 165	2 655
Total, consolidated entities	**1 298**	**1 485**	**1 051**	**1 500**	**1 600**	**2 180**
Contingency reserves	–50	–200	–300	–400	–400	–400
Shortfall to be offset	—	—	430	430	430	430
Exceptional loss – Closure of Gentilly-2	–1 876	—	—	—	—	—
SURPLUS (DEFICIT)	**–2 440**	**1 053**	**1 368**	**1 876**	**2 165**	**2 655**
BALANCED BUDGET ACT						
Payments of revenue dedicated to the Generations Fund	–936	–1 053	–1 368	–1 876	–2 165	–2 655
Exclusion – Exceptional loss	1 876	—	—	—	—	—
BUDGETARY BALANCE(3)	**–1 500**	—	—	—	—	—

(1) This item corresponds to the revenue and expenditure of the general fund.
(2) Includes consolidation adjustments.
(3) Budgetary balance within the meaning of the *Balanced Budget Act.*

1.5.2 Consolidated results

The following table presents the government's consolidated financial framework. The consolidated budgetary transactions provide complete information on the government's fiscal framework.

TABLE B.15

Consolidated financial framework for adjusted revenue and expenditure
Results consolidated by sector – March 2013
(millions of dollars)

	2012-2013	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
Revenue						
General fund	68 652	72 109	74 133	76 500	78 949	81 260
Special funds	8 882	9 874	9 795	10 422	10 885	11 437
Generations Fund	936	1 053	1 368	1 876	2 165	2 655
Non-budget-funded bodies	19 072	19 827	20 554	21 921	22 758	23 679
Health and social services and education networks	36 640	37 753	38 906	40 094	41 665	43 084
Specified purpose accounts	1 173	1 077	1 161	958	958	958.
Tax-funded transfers(1)	6 174	6 202	6 282	6 398	6 489	6 488
Consolidation adjustments(2)	–51 135	–52 841	–54 823	–57 465	–60 045	–62 133
Consolidated revenue	**90 394**	**95 054**	**97 376**	**100 704**	**103 824**	**107 428**
Expenditure						
General fund	–62 642	–63 825	–65 411	–67 502	–69 665	–71 881
Special funds	–7 521	–8 270	–8 520	–8 782	–8 957	–9 175
Non-budget-funded bodies	–17 547	–18 334	–19 084	–20 303	–21 042	–21 750
Health and social services and education networks	–35 883	–36 842	–37 908	–38 898	–40 304	–41 677
Specified purpose accounts	–1 173	–1 077	–1 161	–958	–958	–958
Tax-funded expenditure(1)	–6 174	–6 202	–6 282	–6 398	–6 489	–6 488
Consolidation adjustments(2)	49 979	51 516	53 212	55 423	57 577	59 558
Consolidated expenditure excluding debt service	**–80 961**	**–83 034**	**–85 154**	**–87 418**	**–89 838**	**–92 371**
Debt service						
General fund	–7 822	–8 516	–8 535	–8 652	–8 749	–8 934
Consolidated entities(3)	–2 125	–2 251	–2 449	–2 788	–3 102	–3 498
Consolidated debt service	**–9 947**	**–10 767**	**–10 984**	**–11 440**	**–11 851**	**–12 432**
Consolidated expenditure	**–90 908**	**–93 801**	**–96 138**	**–98 858**	**–101 689**	**–104 803**
Contingency reserves	–50	–200	–300	–400	–400	–400
Exceptional loss – Closure of Gentilly-2	–1 876	—	—	—	—	—
Shortfall to be offset	—	—	430	430	430	430
SURPLUS (DEFICIT)	**–2 440**	**1 053**	**1 368**	**1 876**	**2 165**	**2 655**
BALANCED BUDGET ACT						
Payments of revenue dedicated to the Generations Fund	–936	–1 053	–1 368	–1 876	–2 165	–2 655
Exclusion – Exceptional loss	1 876	—	—	—	—	—
BUDGETARY BALANCE(4)	**–1 500**	**—**	**—**	**—**	**—**	**—**

(1) Doubtful tax accounts are included.
(2) Consolidation adjustments stem mainly from the elimination of reciprocal transactions between entities in different sectors.
(3) Includes consolidation adjustments.
(4) Budgetary balance within the meaning of the *Balanced Budget Act.*

1.6 Public capital investment

In Budget 2013-2014, the government announced the following policy directions respecting public capital investment:

— the maximum level of all public capital investment has been set until 2025-2026;

— the government has committed itself to improving the planning and management of infrastructure overall.

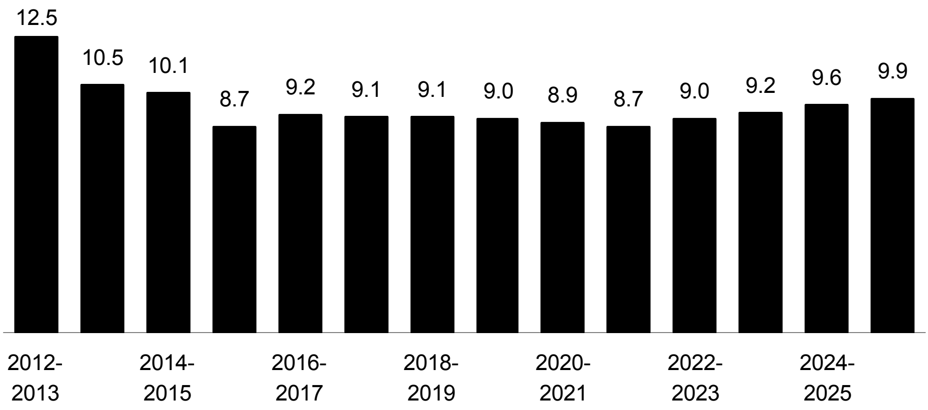
■ Infrastructure investment targets

Government investments will total $10.5 billion in 2013-2014 by including all capital investments financed by government entities.

The Chair of the Conseil du trésor will subsequently make public the details of public capital investment, in particular by sector and type of investment.

CHART B.4

Maximum budget allowances for all public capital investment[(1)]
(billions of dollars)



(1) This is the capital investment financed by the government, including investments made by government entities, i.e. government departments and bodies and non-governmental entities.

Section C

THE QUÉBEC GOVERNMENT'S DEBT

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INTRODUCTION

Several concepts of debt can be used to measure a government's indebtedness. The following table presents data on the debt according to three concepts, i.e. gross debt, net debt and debt representing accumulated deficits.

TABLE C.1

Debt of the Québec government as at March 31
(millions of dollars)

	2012	2013P	2014P	2015P	2016P	2017P	2018P
GROSS DEBT(1)	**183 384**	**193 641**	**197 078**	**201 839**	**204 637**	**206 227**	**207 983**
As a % of GDP	*53.0(2)*	*54.2*	*53.2*	*52.5*	*51.2*	*49.8*	*48.5*
Less: Financial assets, net of other liabilities	–16 273	–17 066	–16 410	–14 339	–14 686	–14 241	–15 563
NET DEBT	**167 111**	**176 575**	**180 668**	**187 500**	**189 951**	**191 986**	**192 420**
As a % of GDP	*48.3(2)*	*49.4*	*48.8*	*48.8*	*47.5*	*46.3*	*44.9*
Less: Non-financial assets	–52 989	–58 806	–63 952	–68 852	–73 179	–77 379	–80 468
DEBT REPRESENTING ACCUMULATED DEFICITS	**114 122**	**117 769**	**116 716**	**118 648**	**116 772**	**114 607**	**111 952**
As a % of GDP	*33.0(2)*	*32.9*	*31.5*	*30.9*	*29.2*	*27.7*	*26.1*

P: Preliminary results for 2013 and forecasts for subsequent years.
(1) The gross debt excludes pre-financing and takes into account the sums accumulated in the Generations Fund.
(2) Compared to the November 2012 budget, debt-to-GDP ratios have been adjusted downward because of new GDP data released by Statistics Canada in November 2012. The ratio of the gross debt to GDP has been adjusted downward by 1.6 percentage points (from 54.6% to 53.0%), that of the net debt to GDP by 1.5 percentage points (from 49.8% to 48.3%) and that of the debt representing accumulated deficits to GDP by 1.0 percentage point (from 34.0% to 33.0%).

1. GROSS DEBT

Gross debt represents the amount of debt contracted on the financial markets and the net liabilities in respect of the retirement plans and future benefits of public and parapublic sector employees, minus the balance of the Generations Fund.

As at March 31, 2013, the gross debt should reach $193 641 million, or 54.2% of GDP. As of 2013-2014, the ratio of gross debt to GDP should gradually decline to 48.5% as at March 31, 2018.

TABLE C.2

Gross debt as at March 31
(millions of dollars)

	2012	2013P	2014P	2015P	2016P	2017P	2018P
Consolidated direct debt(1)	158 887	170 625	173 810	179 664	184 331	188 334	193 470
Plus: Net retirement plans liability	28 727	28 229	28 834	29 109	29 116	28 868	28 143
Plus: Net employee future benefits liability	47	—	—	—	—	—	—
Less: Generations Fund	–4 277	–5 213	–5 566	–6 934	–8 810	–10 975	–13 630
GROSS DEBT(1)	**183 384**	**193 641**	**197 078**	**201 839**	**204 637**	**206 227**	**207 983**
As a % of GDP	***53.0***	***54.2***	***53.2***	***52.5***	***51.2***	***49.8***	***48.5***

P: Preliminary results for 2013 and forecasts for subsequent years.
(1) The consolidated direct debt and the gross debt exclude pre-financing.

Retirement plans liability

The net retirement plans liability is calculated by subtracting from the retirement plans liability the balance of the Retirement Plans Sinking Fund (RPSF), an asset established to pay the retirement benefits of public and parapublic sector employees.

The retirement plans liability represents the present value of the retirement benefits that the government will pay to public and parapublic sector employees, taking into account the conditions of their plans and their years of service. This liability should reach $76 573 million as at March 31, 2013.

The government created the RPSF in 1993. As at March 31, 2013, the book value of the RPSF should stand at $48 344 million.

The net retirement plans liability should thus represent $28 229 million as at March 31, 2013.

Net retirement plans liability as at March 31, 2013^{P}
(millions of dollars)

Retirement plans liability	
Government and Public Employees Retirement Plan (RREGOP)	45 754
Pension Plan of Management Personnel (PPMP) and Retirement Plan for Senior Officials (RPSO)	10 642
Other plans(1)	20 177
Subtotal	**76 573**
Less: Retirement Plans Sinking Fund	–48 344
NET RETIREMENT PLANS LIABILITY	**28 229**

P: Preliminary results.
(1) The liability for the other plans takes into account the assets of the other plans, including those of the Pension Plan of the Université du Québec.

Employee future benefits liability

The government records in its debt the value of its commitments regarding future benefits programs for its employees, namely, programs for accumulated sick leave and for pensions paid to the survivors of government employees. These programs give rise to long-term obligations whose costs are covered in full by the government.

As at March 31, 2013, the employee future benefits liability should stand at $1 249 million.

As at March 31, 2013, the value of the sums accumulated to pay for employee future benefits programs (Accumulated Sick Leave Fund and Survivor's Pension Plan Fund) should reach $1 249 million.

Taking these funds into account, the net employee future benefits liability should be nil as at March 31, 2013.

Net employee future benefits liability as at March 31, 2013[P]
(millions of dollars)

Employee future benefits liability	
Accumulated sick leave	666
Survivor's pension plan	409
Université du Québec programs	174
Subtotal	**1 249**
Less:	
Accumulated Sick Leave Fund	–798
Survivor's Pension Plan Fund	–451
Subtotal	**–1 249**
NET EMPLOYEE FUTURE BENEFITS LIABILITY	**0**

P: Preliminary results.

Generations Fund

The Generations Fund was created in June 2006 through the adoption of the *Act to reduce the debt and establish the Generations Fund.* The sums accumulated in the fund are dedicated solely to repaying the debt.

As at March 31, 2013, the book value of the Generations Fund should stand at $5 213 million.

The sums accumulated in the Generations Fund should reach $13 630 million as at March 31, 2018.

Generations Fund
(millions of dollars)

	2011-2012	2012-2013P	2013-2014P	2014-2015P	2015-2016P	2016-2017P	2017-2018P
Book value, beginning of year	**3 437**	**4 277**	**5 213**	**5 566**	**6 934**	**8 810**	**10 975**
Dedicated revenues							
Water-power royalties							
Hydro-Québec	591	627	666	648	667	682	699
Private producers	91	92	92	94	96	98	100
	682	719	758	742	763	780	799
Indexation of the price of heritage pool electricity	—	—	—	95	190	290	395
Mining royalties	—	—	—	25	315	360	360
Tax on alcoholic beverages	—	—	—	100	100	100	100
Savings related to the closure of Gentilly-2	—	—	—	—	—	—	215
Unclaimed property	9	12	12	12	12	12	12
Investment income	149	205	283	394	496	623	774
Total dedicated revenues	**840**	**936**	**1 053**	**1 368**	**1 876**	**2 165**	**2 655**
Deposit coming from the Territorial Information Fund	—	—	300	—	—	—	—
Total deposits	**840**	**936**	**1 353**	**1 368**	**1 876**	**2 165**	**2 655**
Use of Generations Fund to repay maturing borrowings	—	—	–1 000	—	—	—	—
Book value, end of year	**4 277**	**5 213**	**5 566**	**6 934**	**8 810**	**10 975**	**13 630**

P: Preliminary results for 2012-2013 and forecasts for subsequent years.

❑ Factors responsible for growth in the gross debt

In 2012-2013, the gross debt should increase by $10 257 million, mainly because of capital investments ($5 817 million) and the budget deficit ($3 376 million including the extraordinary loss of $1 876 million stemming from the closure of the Gentilly-2 nuclear power plant).

The table on the following page presents in detail the factors responsible for growth in the government's gross debt since March 31, 2000.

TABLE C.3

Factors responsible for growth in the Québec government's gross debt

(millions of dollars)

	Debt, beginning of year	Budget deficit (surplus)	Investments, loans and advances	Net investment in the networks[1]	Net capital investments[2]	Other factors[3]	Generations Fund[4]	Total change	Debt, end of year	As a % of GDP
With networks consolidated at modified equity value										
2000-2001	116 761	–427	1 701	841	578	1 108		3 801	120 562	53.6
2001-2002	120 562	–22	1 248	934	1 199	–9		3 350	123 912	53.5
2002-2003	123 912	728	1 921	631	1 706	237		5 223	129 135	53.5
2003-2004	129 135	358	1 367	560	1 186	625		4 096	133 231	53.1
2004-2005	133 231	664	1 303	1 486	1 006	–796		3 663	136 894	52.1
2005-2006	136 894	–37	1 488	1 013	1 179	–809		2 834	139 728	51.4
2006-2007	139 728	–109	2 213	1 002	1 177	1 078	–584	4 777	144 505	51.2
2007-2008	144 505	—	2 658	487	1 457	767	–649	4 720	149 225	48.7
2008-2009	149 225	—	966	622	2 448	–28	–719	3 289	152 514	48.6
With networks consolidated line by line[5]										
2009-2010	157 630	3 174	1 746		4 226	–2 733	–725	5 688	163 318	51.6
2010-2011	163 318	3 150	2 507		4 923	298	–760	10 118	173 436	52.5
2011-2012	173 436	2 628	1 888		5 350	922	–840	9 948	183 384	53.0
2012-2013	183 384	3 376[6]	486		5 817	1 514	–936	10 257	193 641	54.2
2013-2014	193 641	—	1 575		5 146	–1 931	–1 353	3 437	197 078	53.2
2014-2015	197 078	—	1 297		4 900	–68	–1 368	4 761	201 839	52.5
2015-2016	201 839	—	1 341		4 327	–994	–1 876	2 798	204 637	51.2
2016-2017	204 637	—	1 493		4 200	–1 938	–2 165	1 590	206 227	49.8
2017-2018	206 227	—	1 520		3 089	–198	–2 655	1 756	207 983	48.5

(1) The net investment in the networks includes mainly loans by Financement-Québec and the Corporation d'hébergement du Québec to institutions in the health and social services and education networks. Since 2009-2010, these items have been part of net capital investments.
(2) Investments made under private-public partnership agreements are included in net capital investments.
(3) Other factors include in particular the change in other accounts, such as accounts receivable and accounts payable.
(4) Deposits in the Generations Fund in 2013-2014 include $1 053 million in dedicated revenues and $300 million coming from the accumulated surplus of the Territorial Information Fund.
(5) The line-by-line consolidation of the financial statements of institutions in the health and social services and education networks raised the gross debt by $5 116 million as at March 31, 2009. This amount represents the debt contracted by the networks in their own name. The data prior to 2009-2010 could not be restated and are thus not comparable.
(6) The budgetary deficit includes the extraordinary loss of $1 876 million stemming from the closure of the Gentilly-2 nuclear power plant. The impact on the gross debt amounts to $1 407 million, which corresponds to the decrease in the dividend paid to the government by Hydro-Québec (75% of $1 876 million).

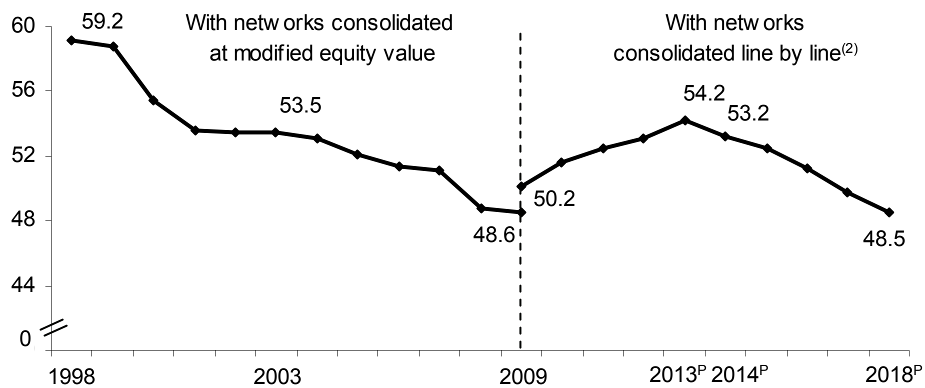
❑ Gross debt burden

Between 1998 and 2009, the government's gross-debt-to-GDP ratio fell significantly. While the gross debt was equivalent to 59.2% of GDP as at March 31, 1998, this ratio stood at 53.5% as at March 31, 2003 and 48.6% as at March 31, 2009. The line-by-line consolidation of the network institutions' financial statements with those of the government raised the debt-to-GDP ratio to 50.2% as at March 31, 2009.

The ratio has risen since 2009 mainly because of the increase in capital expenditures and the recession of 2008-2009. The debt burden is expected to decrease as of 2013-2014.

CHART C.1

Gross debt as at March 31(1)
(as a percentage of GDP)



P: Preliminary results for 2013 and forecasts for subsequent years.
(1) The gross debt excludes pre-financing and takes into account the sums accumulated in the Generations Fund.
(2) The gross debt takes into account the debt that the health and social services and education networks have contracted in their own name. Therefore, the data as of 2009 are not comparable with those for previous years since they do not include this debt.

2. NET DEBT

Net debt is equivalent to the Québec government's liabilities less its financial assets. It represents the debt that has funded capital investments and current expenditures. Net debt is obtained by subtracting from the gross debt the government's financial assets, net of other liabilities.

As at March 31, 2013, the net debt should reach $176 575 million, or 49.4% of GDP. Net debt as a proportion of GDP will start to decrease as of 2013-2014.

TABLE C.4

Factors responsible for growth in the net debt
(millions of dollars)

	Debt, beginning of year	Budgetary deficit	Net capital investments	Impact of the closure of Gentilly-2	Deposits to the Generations Fund	Other	Total change	Debt, end of year	As a % of GDP
2011-2012	159 333	2 628	5 350		–840	640(1)	7 778	167 111	48.3
2012-2013P	167 111	1 500	5 817	1 876	–936	1 207(2)	9 464	176 575	49.4
2013-2014P	176 575	—	5 146		–1 053	—	4 093	180 668	48.8
2014-2015P	180 668	—	4 900		–1 368	3 300(3)	6 832	187 500	48.8
2015-2016P	187 500	—	4 327		–1 876	—	2 451	189 951	47.5
2016-2017P	189 951	—	4 200		–2 165	—	2 035	191 986	46.3
2017-2018P	191 986	—	3 089		–2 655	—	434	192 420	44.9

P: Preliminary results for 2012-2013 and forecasts for subsequent years.
(1) Includes, in particular, changes stemming from inventories and prepaid expenses that are non-financial assets.
(2) In 2012-2013, the net debt will be adjusted by $1 207 million because of the new accounting standard applicable to transfer payments under which the Société de financement des infrastructures locales du Québec (SOFIL) and the Société d'habitation du Québec (SHQ) are to modify their method of accounting for subsidies in respect of debt service. This modification will have the same impact on the debt representing accumulated deficits as at March 31, 2013.
(3) Reserve for the impact of the eventual transition of Hydro-Québec to International Financial Reporting Standards. This provision is explained in the following pages.

3. DEBT REPRESENTING ACCUMULATED DEFICITS

The debt representing accumulated deficits corresponds to the difference between the government's liabilities and its financial and non-financial assets as a whole. This debt is calculated by subtracting financial assets, net of other liabilities, as well as non-financial assets from the gross debt.

As at March 31, 2013, the debt representing accumulated deficits should stand at $117 769 million, or 32.9% of GDP. As a proportion of GDP, the debt representing accumulated deficits will decline as of 2012-2013.

TABLE C.5

Factors responsible for growth in the debt representing accumulated deficits
(millions of dollars)

	Debt, beginning of year	Budgetary deficit	Impact of the closure of Gentilly-2	Deposits to the Generations Fund	Other	Total change	Debt, end of year	As a % of GDP
2011-2012	111 946	2 628		–840	388	2 176	114 122	33.0
2012-2013P	114 122	1 500	1 876	–936	1 207(1)	3 647	117 769	32.9
2013-2014P	117 769	—		–1 053	—	–1 053	116 716	31.5
2014-2015P	116 716	—		–1 368	3 300	1 932	118 648	30.9
2015-2016P	118 648	—		–1 876	—	–1 876	116 772	29.2
2016-2017P	116 772	—		–2 165	—	–2 165	114 607	27.7
2017-2018P	114 607	—		–2 655	—	–2 655	111 952	26.1

P: Preliminary results for 2012-2013 and forecasts for subsequent years.
(1) This amount corresponds to the restatement stemming from the new accounting standard for transfer payments.

The debt representing accumulated deficits in 2014-2015 takes into account a reserve for the impact of the eventual transition of Hydro-Québec to International Financial Reporting Standards (IFRS). Since the November 2012 budget, the Canadian Institute of Chartered Accountants (CICA) has again postponed the date of the mandatory changeover to the IFRS for corporations like Hydro-Québec that engage in rate-regulated activities. The anticipated date is now January 1, 2015, which would affect the government's 2014-2015 fiscal year.

Based on information as at December 31, 2012, the impact of Hydro-Québec's changeover to the IFRS would be roughly $6 billion. However, it should be noted that enterprises similar to Hydro-Québec in British Columbia and Ontario (BC Hydro and Hydro One) have adopted American accounting standards for their rate-regulated activities instead of the IFRS. Given the uncertainty surrounding the final impact of the change in accounting standards for Hydro-Québec, it has been decided to maintain the restatement at $3.3 billion, indicated in the March and November 2012 budgets, but to apply it in 2014-2015. It should be noted that Hydro-Québec's eventual transition to the IFRS will not have any impact on the government's gross debt.

4. DEBT REDUCTION OBJECTIVES

In its November 20, 2012 budget, the government confirmed that it was maintaining the debt reduction objectives included in the *Act to reduce the debt and establish the Generations Fund*:

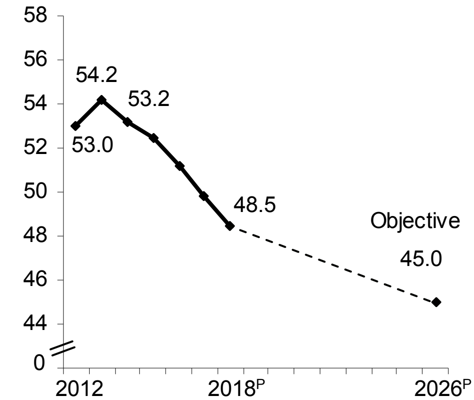
— 45% of GDP for the gross debt as at March 31, 2026;

— 17% of GDP for the debt representing accumulated deficits as at March 31, 2026.

CHART C.2

Gross debt as at March 31

(as a percentage of GDP)



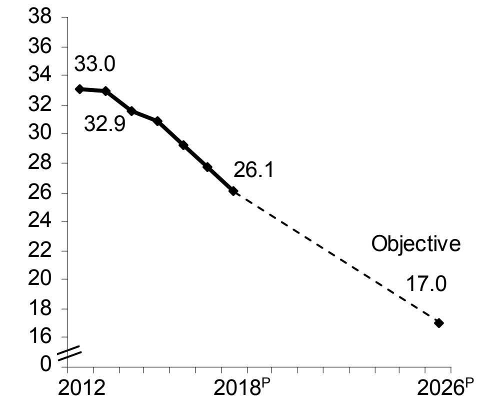
P: Preliminary results for 2013, forecasts for 2014 to 2018 and projections for subsequent years.

Note: The gross debt excludes pre-financing and takes into account the sums accumulated in the Generations Fund.

CHART C.3

Debt representing accumulated deficits as at March 31

(as a percentage of GDP)



P: Preliminary results for 2013, forecasts for 2014 to 2018 and projections for subsequent years.

To achieve the debt reduction objectives, the government announced in last November's budget that it will deposit in the Generations Fund:

— The revenue that will be generated by the indexation of the price of heritage pool electricity starting in 2014, which will represent $95 million in 2014-2015, $190 million in 2015-2016, $290 million in 2016-2017 and $395 million in 2017-2018;

— All mining royalties as of 2015-2016, which will represent $315 million in 2015-2016 and $360 million per year subsequently;

— The revenue, as of 2017-2018, that will stem from the increase in Hydro-Québec's net earnings as a result of the closure of the Gentilly-2 nuclear power plant, which will represent $215 million per year;

— An amount of $100 million per year, as of 2014-2015, that will be generated by the increase in the specific tax on alcoholic beverages.

The government also announced a $1.5 billion annual reduction as of 2013-2014 in planned capital investments.

These debt reduction measures will enable the government to achieve the objectives set in the *Act to reduce the debt and establish the Generations Fund.*

Lastly, the government will use $1 billion from the Generations Fund in 2013-2014 to repay maturing borrowings. The use of $1 billion from the Generations Fund will reduce the consolidated direct debt, i.e. the debt contracted on financial markets, by an equivalent amount. However, this will not have an impact on the gross debt, because the Generations Fund is subtracted from the gross debt. This debt repayment will make it possible to save some $25 million in 2013-2014 and $40 million per year afterwards on debt service.

Owing to these new revenue sources, which are over and above those currently dedicated to the Generations Fund, this fund should total $13.6 billion as at March 31, 2018.

5. PUBLIC SECTOR DEBT

Public sector debt includes the government's gross debt as well as the debt of Hydro-Québec, municipalities, universities other than the Université du Québec and its constituents, and other government enterprises. This debt has served notably to finance public infrastructure, such as roads, schools, hospitals, hydroelectric dams and water treatment plants.

As at March 31, 2013, Québec's public sector debt should stand at $258 592 million, or 72.3% of GDP. These figures must be put into perspective for they do not take into account the economic value of certain assets held by the government, such as Hydro-Québec, the Société des alcools du Québec and Loto-Québec.

TABLE C.6

Public sector debt as at March 31
(millions of dollars)

	2010	2011	2012	2013P
Government's gross debt(1)	163 318	173 436	183 384	193 641
Hydro-Québec	36 385	37 723	38 514	39 492
Municipalities(2)	19 538	20 307	20 719	22 201
Universities other than the Université du Québec and its constituents(3)	1 930	1 925	1 797	1 797
Other government enterprises(4)	697	1 363	1 363	1 461
PUBLIC SECTOR DEBT	**221 868**	**234 754**	**245 777**	**258 592**
As a % of GDP	***70.2***	***71.1***	***71.1***	***72.3***

P: Preliminary results.
(1) The gross debt excludes pre-financing and takes into account the sums accumulated in the Generations Fund.
(2) These amounts correspond to the long-term debt contracted by municipalities in their own name. Part of this debt is subsidized by the government ($4 377 million as at March 31, 2013).
(3) These amounts correspond to the debt contracted by universities other than the Université du Québec and its constituents in their own name. Part of this debt is subsidized by the government ($137 million as at March 31, 2013).
(4) These amounts correspond to the debt contracted by the Financing Fund to finance government enterprises and entities not included in the reporting entity.

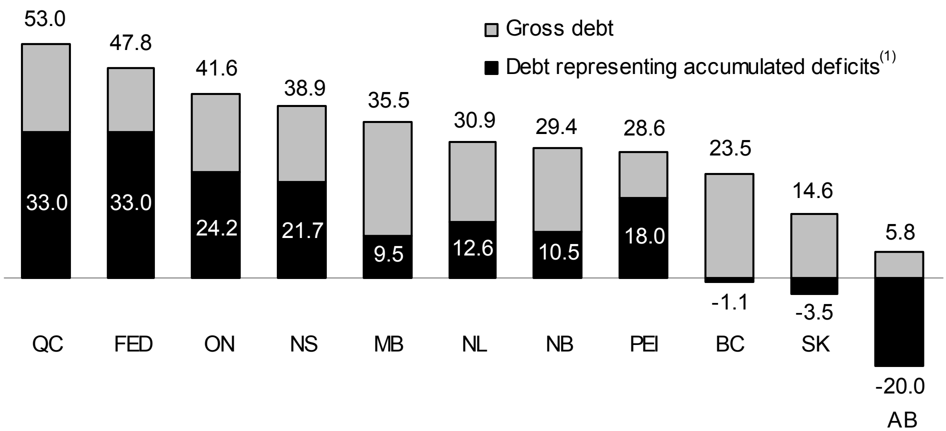
6. COMPARISON OF THE DEBT OF GOVERNMENTS IN CANADA

Be it on the basis of the gross debt or on that of the debt representing accumulated deficits, as a percentage of GDP, Québec is the most heavily indebted province.

As at March 31, 2012, the ratio of gross debt to GDP was 53.0% in Québec, compared with 41.6% in Ontario, second among the most indebted provinces, and 38.9% in Nova Scotia, which ranks third.

CHART C.4

Gross debt and debt representing accumulated deficits as at March 31, 2012
(as a percentage of GDP)



(1) A negative entry means that the government has an accumulated surplus.
Sources: Governments' public accounts, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

The table on the following page shows the debt of the federal government and each of the provinces as at March 31, 2012. The boxes indicate the concept of debt used by each government in its budget documents to measure its debt level. Some governments use more than one concept.

Contrary to net debt and debt representing accumulated deficits, gross debt is not a concept that can be observed directly in the public accounts of the other governments in Canada. However, the public accounts show the components of the gross debt, i.e. the consolidated direct debt, the net retirement plans liability and the net employee future benefits liability. It is possible, therefore, to calculate the level of the gross debt.

TABLE C.7

Debt as at March 31, 2012 according to various concepts
(millions of dollars)

	QC	FED	ON	BC	AB	NB	NL	MB	SK	NS	PEI
Consolidated direct debt	**158 887**	**633 285**	**267 471**	**49 463**	**6 692**	**9 371**	**5 202**	**17 788**	**4 628**	**12 665**	**1 434**
Net retirement plans liability	28 727	148 911	–6 313	110	10 556	–260	3 090	1 634	6 317	102	96
Net employee future benefits liability	47	60 515	11 115	1 690		339	2 083	413		1 622	3
Generations Fund	–4 277										
Gross debt	**183 384**	**842 711**	**272 273**	**51 263**	**17 248**	**9 450**	**10 375**	**19 835**	**10 945**	**14 389**	**1 533**
As a % of GDP	*53.0*	*47.8*	*41.6*	*23.5*	*5.8*	*29.4*	*30.9*	*35.5*	*14.6*	*38.9*	*28.6*
Less: Financial assets, net of other liabilities	–16 273	–192 576	–36 691	–15 290	–36 239	596	–2 550	–5 324	–6 402	–1 146	318
Net debt[(1)]	**167 111**	**650 135**	**235 582**	**35 973**	**–18 991**	**10 046**	**7 825**	**14 511**	**4 543**	**13 243**	**1 851**
As a % of GDP	*48.3*	*36.9*	*36.0*	*16.5*	*–6.4*	*31.2*	*23.3*	*26.0*	*6.1*	*35.8*	*34.6*
Less: Non-financial assets	–52 989	–67 959	–77 172	–38 430	–40 122	–6 678	–3 582	–9 206	–7 160	–5 203	–887
Debt representing accumulated deficits[(1)]	**114 122**	**582 176**	**158 410**	**–2 457**	**–59 113**	**3 368**	**4 243**	**5 305**	**–2 617**	**8 040**	**964**
As a % of GDP	*33.0*	*33.0*	*24.2*	*–1.1*	*–20.0*	*10.5*	*12.6*	*9.5*	*–3.5*	*21.7*	*18.0*

Note: The boxes indicate the debt concept(s) used in the budget documents of the governments concerned.
(1) A negative entry indicates that the government has net assets or an accumulated surplus.
Sources: Governments' public accounts, Statistics Canada and Ministère des Finances et de l'Économie du Québec.

APPENDIX 1: INFORMATION ON FINANCING AND DEBT MANAGEMENT

1.1 The financing program

Based on preliminary results, the 2012-2013 financing program should stand at $20 121 million, up $2 818 million in relation to what was forecast in the November 2012 budget.

This increase stems mainly from the $1 billion in deposits to the Retirement Plans Sinking Fund (RPSF) and $2.6 billion in pre-financing to take advantage of favourable market conditions. Moreover, additional contributions of $860 million were made to the Sinking Fund for government borrowings within the framework of the government policy aimed at increasing its prudential liquidity (see page C.31 for more details).

TABLE C.8

The government's financing program in 2012-2013P
(millions of dollars)

	November 2012 budget	Revisions	Revised program
GENERAL FUND			
Net financial requirements[(1),(2)]	4 545	375	4 920
Repayments of borrowings	4 623	42	4 665
Change in cash position[(3)]	–4 436	—	–4 436
Deposits in the Retirement Plans Sinking Fund or retirement plans[(4)]	—	1 149	1 149
Transactions under the credit policy[(5)]	471	–818	–347
Additional contributions to the Sinking Fund for borrowings	3 000	860	3 860
Subtotal	**8 203**	**1 608**	**9 811**
Pre-financing	—	2 646	2 646
GENERAL FUND	**8 203**	**4 254**	**12 457**
FINANCING FUND	**5 100**	**–1 022**	**4 078**
Subtotal - General fund and Financing Fund	**13 303**	**3 232**	**16 535**
FINANCEMENT-QUÉBEC	**4 000**	**–414**	**3 586**
TOTAL	**17 303**	**2 818**	**20 121**
Including: repayments of borrowings[(6)]	7 743	42	7 785

P: Preliminary results based on borrowings carried out or negotiated as at March 22, 2013.
Note: A negative entry indicates a source of financing and a positive entry, a financial requirement.
(1) These amounts exclude the net financial requirements of the consolidated entities, which are financed through Financing Fund and Financement-Québec financing programs.
(2) Net financial requirements are adjusted to take into account the non-receipt of RPSF revenues and of funds dedicated to employee future benefits.
(3) Corresponds to pre-financing made in 2011-2012.
(4) Deposits in the RPSF are optional.
(5) Under its credit policy, which is designed to limit financial risk with respect to counterparties, the government received $347 million in 2012-2013 because of the change in foreign exchange rates.
(6) Includes repayments of borrowings of the general fund ($4 665 million), the Financing Fund ($1 254 million) and Financement-Québec ($1 866 million).

The financing program should stand at $11 671 million in 2013-2014 and $17 549 million in 2014-2015.

TABLE C.9

The government's financing program in 2013-2014 and 2014-2015
(millions of dollars)

	2013-2014F	2014-2015F
GENERAL FUND		
Net financial requirements(1),(2)	–392	400
Repayments of borrowings	4 569	7 649
Use of the Generations Fund to repay maturing borrowings	–1 000	—
Change in cash position(3)	–2 646	—
Deposits in the Retirement Plans Sinking Fund or retirement plans(4)	—	—
Additional contributions to the Sinking Fund for borrowings	2 140	—
GENERAL FUND	**2 671**	**8 049**
FINANCING FUND	**8 000**	**8 500**
Subtotal - General fund and Financing Fund	**10 671**	**16 549**
FINANCEMENT-QUÉBEC	**1 000**	**1 000**
TOTAL	**11 671**	**17 549**
Including: repayments of borrowings(5)	9 538	12 290

F: Forecasts.
Note: A negative entry indicates a source of financing and a positive entry, a financial requirement.
(1) These amounts exclude the net financial requirements of the consolidated entities, which are financed through Financing Fund financing program.
(2) Net financial requirements are adjusted to take into account the non-receipt of RPSF revenues and of funds dedicated to employee future benefits.
(3) Corresponds to pre-financing made in 2012-2013.
(4) Deposits in the RPSF are optional.
(5) Includes repayments of borrowings of the general fund ($4 569 million in 2013-2014 and $7 649 million in 2014-2015), the Financing Fund ($1 247 million in 2013-2014 and $1 130 million in 2014-2015) and Financement-Québec ($3 722 million in 2013-2014 and $3 511 million in 2014-2015).

The anticipated reduction in the financing program in 2013-2014 in relation to the preceding year stems, among other things, from pre-financing in 2012-2013 and the use of $1 billion from the Generations Fund to repay maturing borrowings.

In 2014-2015, the anticipated increase in borrowings in relation to the preceding year stems, in particular, from an increase in repayments of borrowings that year.

Moreover, as of April 1, 2013, the Financing Fund will be responsible for short- and long-term financing of organizations included in the government reporting entity, while Financement-Québec will be responsible for the financing of organizations not included in the government reporting entity.

Consequently, the short-term and long-term borrowings of organizations of the health and social services and the education networks made with Financement-Québec will henceforth be made with the Financing Fund. Financement-Québec will be responsible in particular for the funding of universities other than the Université du Québec and its constituents.

This change will increase the financing program of the Financing Fund by about $4 billion in 2013-2014 and about $5 billion in 2014-2015, but will lead to equivalent reductions in the financing program of Financement-Québec.

1.2 Financing strategy

The government aims to borrow at the lowest possible cost. To that end, it applies a strategy for diversifying sources of funding by market, financial instrument and maturity.

1.2.1 Diversification by market

Financing transactions are conducted regularly on most markets, i.e. in Canada, the United States, Europe and Asia.

From 2002-2003 to 2011-2012, 19% of borrowings were contracted in foreign currency. Nonetheless, the government maintains only a very low exposure of its gross debt to these currencies: the exposure should even be nil as at March 31, 2013.

In 2012-2013, the government contracted 7.8% of its borrowings on foreign markets, i.e.

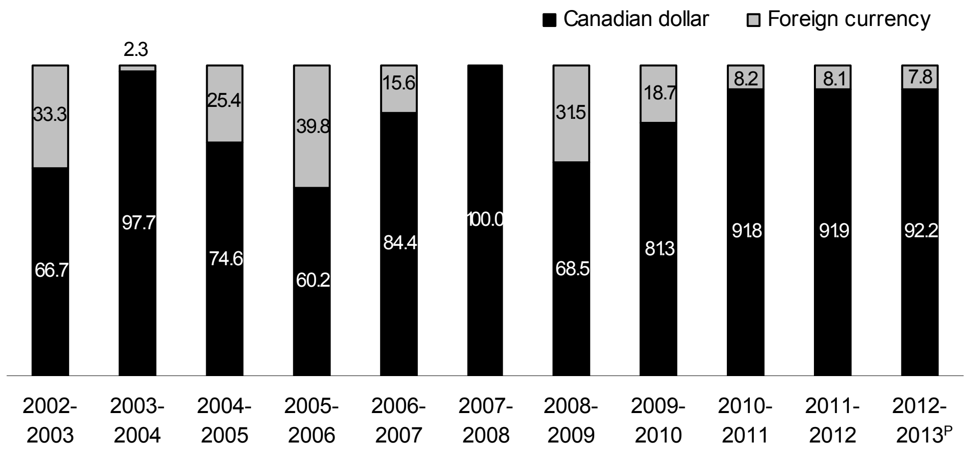
— US$1 250 million (C$1 247 million) in February 2013;

— CHF250 million (C$274 million) in February 2013;

— ¥5 billion (C$53 million) in March 2013.

CHART C.5

Borrowings by currency(1)
(per cent)



P: Preliminary results.
(1) Borrowings of the general fund, borrowings for the Financing Fund and borrowings of Financement-Québec.

1.2.2 Diversification by instrument

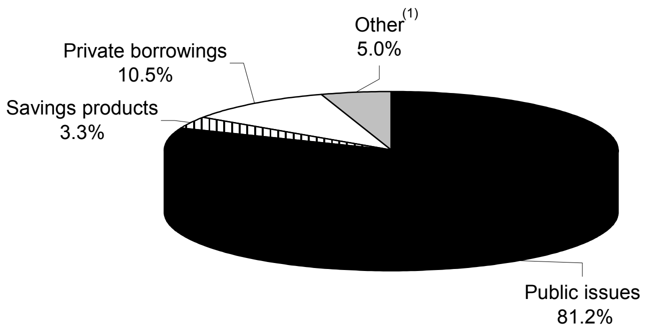
To satisfy investors' needs, an extensive array of financial products is used in the course of financing transactions.

Long-term instruments consist primarily of public bond issues, private borrowings and savings products.

The long-term instruments used in 2012-2013 consist mainly of public issues (81.2%).

CHART C.6

Borrowings in 2012-2013[P] by instrument



P: Preliminary results.
(1) Includes the Business Assistance — Immigrant Investor Program and borrowings from the Canada Pension Plan Investment Fund.

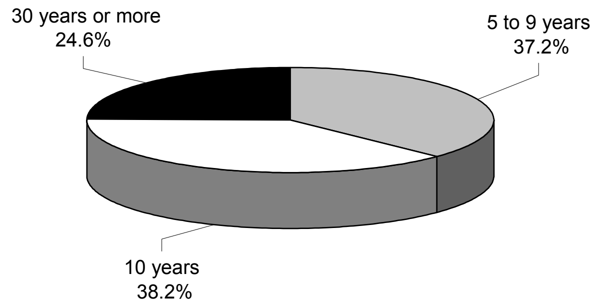
1.2.3 Diversification by maturity

Maturities of new borrowings are distributed over time to obtain a stable refinancing profile and ensure the government's regular presence on capital markets.

In 2012-2013, 37.2% of contracted borrowings had a maturity between 5 and 9 years; 38.2% a maturity of 10 years; and 24.6% a maturity of 30 years or more.

CHART C.7

Borrowings in 2012-2013P by maturity

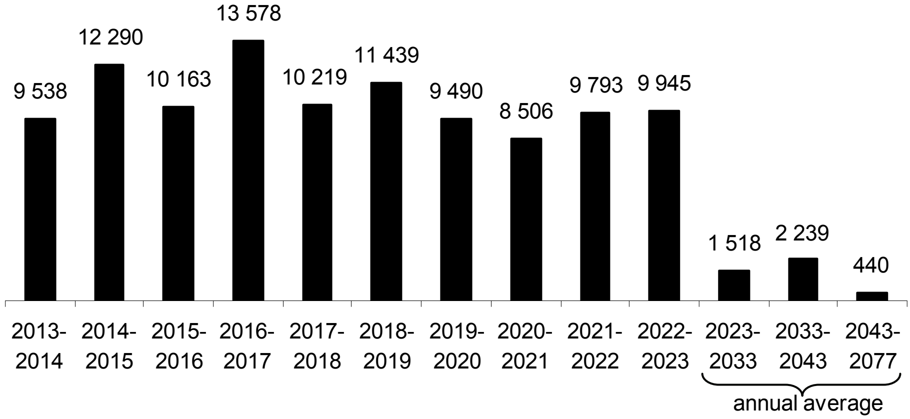


P: Preliminary results.

This diversification by maturity has an impact on the maturity of the debt shown in the following chart. As at March 31, 2013, the average maturity of the debt should stand at 12 years.

CHART C.8

Maturity of the long-term debt as at March 31, 2013P
(millions of dollars)



P: Preliminary results.
Note: Direct debt of the general fund, debt contracted to make advances to the Financing Fund and debt of Financement-Québec.

1.3 Increase in the government's prudential liquidity

As indicated in the March 2012 budget, the Ministère des Finances et de l'Économie implemented in 2012-2013 a new policy aimed at raising the level of prudential liquidity. The goal is to increase the government's liquid assets by $6 billion over two years. These liquid assets will be available for use in the event of major turbulence in financial markets.

The federal government announced a similar policy in its June 2011 budget. Borrowings by the federal government will be increased by $35 billion over three years (2011-2012 to 2013-2014) in order to boost its liquid assets. The federal government recently announced that it expected to complete its prudential liquidity plan by the end of summer 2013, nine months earlier than anticipated. Ontario has also increased its liquid assets substantially in recent years.

In the case of Québec, the $6 billion in additional liquid assets corresponds to roughly one third of the government's annual financing requirements in the coming years.

The $6 billion that is to be borrowed will be deposited into the Sinking Fund for government borrowings, already in existence, and invested in very liquid government short-term securities, such as federal Treasury bills. This will make it possible, in the event of major financial market turbulence where it is difficult to contract short- or long-term borrowings, to sell these securities and rapidly recover the liquid assets. These assets can then be used to buy short-term securities issued by the Québec government, thus enabling it to meet its financial obligations. Once the turbulence is over and the short-term securities issued by the Québec government have matured, the Sinking Fund for government borrowings could again buy short-term securities such as federal Treasury bills.

Since the $6 billion in borrowings over two years will be deposited into the Sinking Fund for government borrowings, there will be no impact on the government's gross debt. This is because the value of a borrowings sinking fund is subtracted from the debt in accordance with accounting standards.

In 2012-2013, $3 860 million was deposited into the Sinking Fund for government borrowings for the purpose of prudential liquidity.

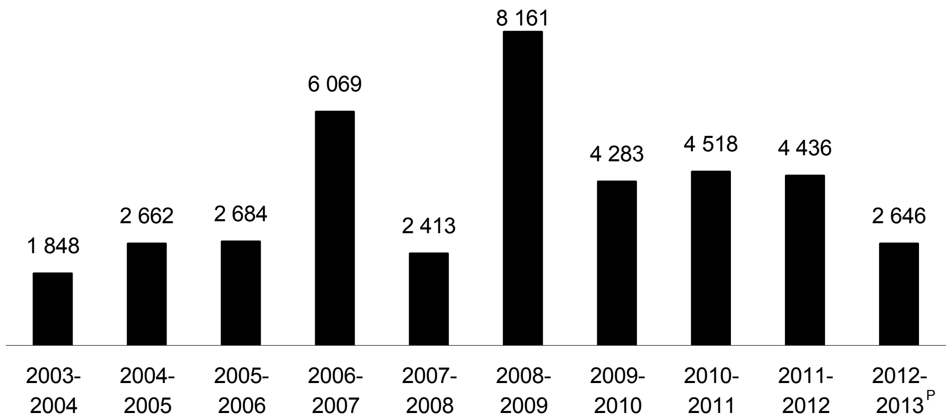
1.4 Pre-financing

The government carries out pre-financing to take advantage of favourable market conditions. These are borrowings that would normally be contracted during the subsequent fiscal year.

Over the past 10 years, the government has contracted, on average, pre-financing of $3 972 million a year.

CHART C.9

Pre-financing
(millions of dollars)



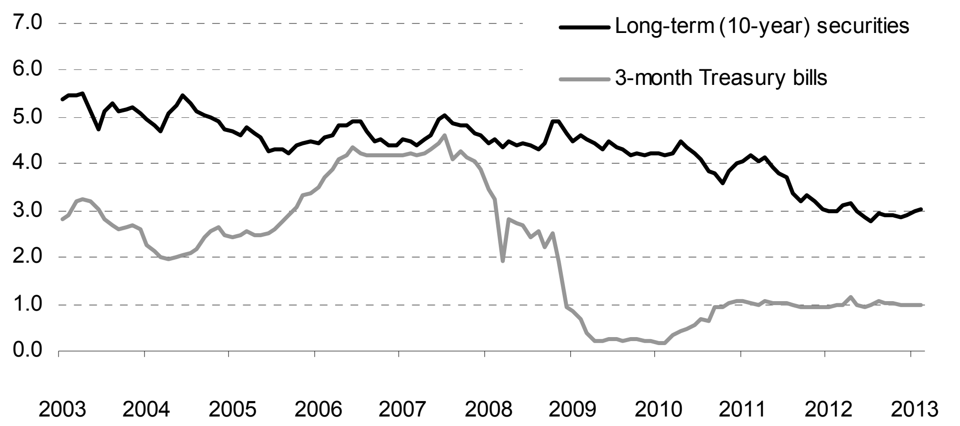
P: Preliminary results.

1.5 Yield

The yield on long-term Québec securities is currently about 3.0%, and short-term interest rates are 1.0%.

CHART C.10

Yield on Québec securities
(per cent)

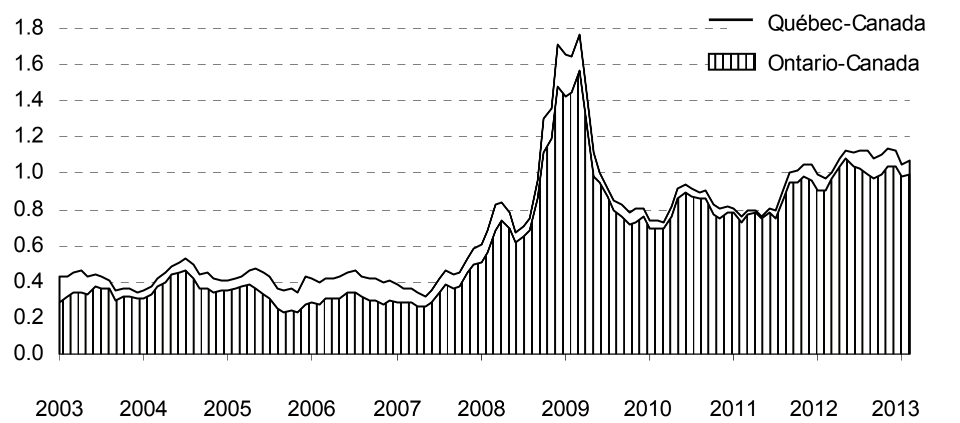


Sources: PC-Bond and Ministère des Finances et de l'Économie du Québec.

In addition, the substantial increase in the spread between the yield on Québec and federal government securities, observed starting in summer 2008 during the financial crisis, has been considerably reduced since then, without returning, however, to the levels observed prior to 2008. The same situation has been observed in the case of the other provinces.

CHART C.11

Yield spread on long-term (10-year) securities
(in percentage points)



Source: PC-Bond.

1.6 Borrowings contracted

TABLE C.10

Québec government
Summary of long-term borrowings contracted[1] in 2012-2013[P]

Currency	$ million	%
CANADIAN DOLLAR		
Public issues	14 805	73.6
Private borrowings	2 064	10.3
Savings products	666	3.3
Business Assistance — Immigrant Investor Program	1 003	5.0
Canada Pension Plan Investment Fund	9	0.0
Subtotal	**18 547**	**92.2**
OTHER CURRENCIES		
US dollar	1 247	6.2
Swiss franc	274	1.4
Yen	53	0.2
Subtotal	**1 574**	**7.8**
TOTAL	**20 121**	**100.0**

P: Preliminary results.
(1) The amounts include the borrowings of the general fund, borrowings for the Financing Fund and borrowings of Financement-Québec.

TABLE C.11

Québec government
Borrowings contracted in 2012-2013P for the general fund

Amount received in Canadian dollars[1]	Face value in foreign currencies	Interest rate[2]	Date of issue	Date of maturity	Price to investor	Yield to investor[3]
(millions)		(%)			($)	(%)
253	—	3.50	April 17	2022-12-01	102.663	3.202
549	—	4.25	April 27	2043-12-01	109.798	3.720
415	—	3.50	May 4	2022-12-01	103.008	3.163
454	—	4.25	May 8	2043-12-01	110.707	3.674
116[4]	—	Various	May 22	2065-06-01	105.648	3.434
222	—	3.50	June 12	2022-12-01	104.317	3.016
108[4]	—	Various	June 18	2065-06-01	107.915	3.316
499	—	3.50	June 26	2022-12-01	104.769	2.965
105	—	3.50	September 25	2022-12-01	105.155	2.911
63	—	4.25	September 28	2043-12-01	114.284	3.494
505	—	4.25	October 16	2043-12-01	112.165	3.597
562	—	4.50	October 19	2017-12-01	112.298	1.962
113[4]	—	Various	November 13	2075-06-01	112.716	3.279
251	—	3.00	December 10	2023-09-01	100.143	2.984
132[4]	—	Various	December 10	2065-06-01	105.607	3.284
566	—	4.25	December 14	2043-12-01	113.227	3.543
446	—	4.25	December 21	2021-12-01	111.461	2.793
497	—	3.00	December 21	2023-09-01	99.390	3.067
334	—	4.25	December 21	2021-12-01	111.293	2.813
491	—	3.00	January 11	2023-09-01	99.394	3.067
333	—	4.25	January 16	2021-12-01	111.080	2.829
561	—	4.25	January 23	2043-12-01	112.107	3.597
1 247	US$1 250	2.625	February 13	2023-02-13	99.590	2.672
274	CHF250	1.125[5]	February 22	2023-02-22	99.976	1.128
315	—	3.00	February 25	2023-09-01	98.376	3.183
560	—	4.25	March 4	2021-12-01	111.907	2.711
206	—	3.00	March 11	2023-09-01	100.348	2.961
549	—	4.25	March 19	2043-12-01	109.706	3.717
53[4]	¥5 000	1.305	March 21	2028-03-21	100.000	1.305
666[6]	—	Various	Various	Various	Various	Various
1 003[7]	—	Zero coupon	Various	Various	Various	Various
9[8]	—	Various	Various	Various	Various	Various
12 457						

P: Preliminary results.
(1) The Canadian equivalent of the value of borrowings in foreign currencies on the date of borrowing is indicated.
(2) Interest payable semi-annually except if another frequency is indicated in a note.
(3) Yield to investor is established on the basis of interest payable semi-annually.
(4) Private borrowings.
(5) Interest is payable annually.
(6) Savings products issued by Épargne Placements Québec.
(7) Business Assistance — Immigrant Investor Program.
(8) Borrowings from the Canada Pension Plan Investment Fund.

TABLE C.12

Québec government
Borrowings contracted in 2012-2013^P for the Financing Fund

Amount received in Canadian dollars(1)	Face value in foreign currencies	Interest rate(2)	Date of issue	Date of maturity	Price to investor	Yield to investor(3)
(millions)		(%)			($)	(%)
A. Borrowings contracted for the consolidated entities						
554	—	4.25	April 3	2043-12-01	110.863	3.667
260	—	3.50	April 17	2022-12-01	102.663	3.202
100	—	3.50	May 4	2022-12-01	103.008	3.163
100	—	4.25	May 8	2043-12-01	110.707	3.674
300	—	3.50	June 12	2022-12-01	104.317	3.016
25	—	3.50	June 26	2022-12-01	104.769	2.965
421	—	3.50	September 25	2022-12-01	105.155	2.911
508	—	4.25	September 28	2043-12-01	114.284	3.494
56	—	4.25	October 16	2043-12-01	112.165	3.597
450	—	3.50	November 6	2022-12-01	105.089	2.913
500	—	3.00	December 5	2023-09-01	99.997	3.000
250	—	3.00	December 10	2023-09-01	100.143	2.984
6	—	3.00	January 11	2023-09-01	99.394	3.067
177	—	3.00	February 25	2023-09-01	98.376	3.183
296	—	3.00	March 11	2023-09-01	100.348	2.961
4 003						
B. Borrowings contracted for entities not included in the reporting entity						
75	—	3.50	November 6	2022-12-01	105.089	2.913
4 078						

P: Preliminary results.
(1) The Canadian equivalent of the value of borrowings in foreign currencies on the date of borrowing is indicated.
(2) Interest payable semi-annually except if another frequency is indicated in a note.
(3) Yield to investor is established on the basis of interest payable semi-annually.

TABLE C.13

Québec government
Borrowings contracted by Financement-Québec in 2012-2013P

Amount received in Canadian dollars (1)	Face value in foreign currency	Interest rate (2)	Date of issue	Date of maturity	Price to investor	Yield to investor(3)
(millions)		(%)			($)	(%)
50(4)	—	Variable (5)	April 20	2017-04-25	99.762	Variable
492	—	2.40	April 24	2018-12-01	98.410	2.664
500	—	2.45	July 13	2019-12-01	99.911	2.463
500	—	2.45	October 10	2019-12-01	100.083	2.437
499	—	2.45	November 30	2019-12-01	99.751	2.489
200(4)	—	Variable (5)	December 12	2018-06-01	100.000	Variable
115(4)	—	Variable (5)	December 12	2018-06-01	100.000	Variable
72(4)	—	Variable (5)	December 12	2018-06-01	100.000	Variable
65(4)	—	Variable (5)	December 12	2018-06-01	100.000	Variable
25(4)	—	Variable (5)	December 12	2018-06-01	100.000	Variable
300(4)	—	Variable (5)	December 20	2018-06-01	100.127	Variable
80(4)	—	Variable (5)	December 20	2018-06-01	100.309	Variable
60(4)	—	Variable (5)	January 10	2018-06-01	100.462	Variable
75(4)	—	Variable (5)	February 11	2018-06-01	100.456	Variable
100(4)	—	Variable (5)	February 19	2018-06-01	100.429	Variable
101(4)	—	Variable (5)	February 20	2018-06-01	100.429	Variable
50(4)	—	Variable (5)	February 20	2018-06-01	100.429	Variable
151(4)	—	Variable (5)	February 21	2018-06-01	100.429	Variable
50(4)	—	Variable (5)	February 25	2018-06-01	100.454	Variable
25(4)	—	Variable (5)	February 25	2018-06-01	100.454	Variable
76(4)	—	Variable (5)	February 25	2018-06-01	100.479	Variable
3 586						

P: Preliminary results.
(1) The Canadian equivalent of the value of borrowings in foreign currencies on the date of borrowing is indicated.
(2) Interest payable semi-annually except if another frequency is indicated in a note.
(3) Yield to investor is established on the basis of interest payable semi-annually.
(4) Private borrowings.
(5) Interest payable quarterly.

TABLE C.14

Borrowings contracted by Hydro-Québec in 2012(1)

Amount received in Canadian dollars(2)	Face value in foreign currency	Interest rate(3)	Date of issue	Date of maturity	Price to investor	Yield to investor(4)
(millions)		(%)			($)	(%)
8	—	Zero coupon	April 25	2017-04-15	88.543	2.476
1 017	US$1 000	1.375	June 19	2017-06-19	99.884	1.399
663	—	5.00	July 24	2050-02-15	132.648	3.444
655	—	5.00	December 4	2050-02-15	130.962	3.504
2 343						

(1) Borrowings contracted from January 1 to December 31, 2012.
(2) The Canadian equivalent of the value of borrowings in foreign currencies on the date of borrowing is indicated.
(3) Interest payable semi-annually except if another frequency is indicated in a note.
(4) Yield to investor is established on the basis of interest payable semi-annually.

1.7 Debt management

The government's debt management strategy aims to minimize the cost of the debt and limit the risks related to fluctuations in foreign exchange and interest rates.

The government uses a range of financial instruments, particularly interest rate and currency swap agreements, to achieve desired debt proportions by currency and interest rate.

❑ Structure of the debt by currency

As at March 31, 2013, the proportion of the government's gross debt in Canadian dollars, after taking into account interest rate and currency swap agreements, should stand at 100.0%. This proportion was 99.8% as at March 31, 2012.

❑ Structure of the debt by interest rate

The government keeps part of its debt at variable rates and part at fixed rates.

After interest rate and currency swap agreements are taken into account, the proportion of the gross debt at floating rates should stand at 11.3% as at March 31, 2013. This proportion was 12.0% as at March 31, 2012.

APPENDIX 2: INFORMATION ON THE RETIREMENT PLANS AND ON FUNDS DEPOSITED BY THE MINISTÈRE DES FINANCES ET DE L'ÉCONOMIE WITH THE CAISSE DE DÉPÔT ET PLACEMENT DU QUÉBEC

2.1 Retirement plans

The Québec government participates financially in the retirement plans of its employees. These plans had 566 983 active participants and 313 962 beneficiaries as at December 31, 2011.

TABLE C.15

Retirement plans of public and parapublic sector employees as at December 31, 2011

	Active participants	Beneficiaries
Government and Public Employees Retirement Plan (RREGOP)	520 000	211 331
Pension Plan of Management Personnel (PPMP) and Retirement Plan for Senior Officials (RPSO)	28 650	24 821
Other plans:		
– Teachers Pension Plan (TPP)(1) and Pension Plan of Certain Teachers (PPCT)(1)	122	46 010
– Civil Service Superannuation Plan (CSSP)(1)	50	21 268
– Superannuation Plan of Members of the Sûreté du Québec (SPMSQ)	5 550	4 836
– Pension Plan of Peace Officers in Correctional Services (PPPOCS)	3 450	1 625
– Pension Plan of the Judges of the Court of Québec and of Certain Municipal Courts (PPJCQM)	273	339
– Pension Plan for Federal Employees Transferred to Employment with the Gouvernement du Québec (PPFEQ)(2)	210	134
– Pension Plan of the Members of the National Assembly (PPMNA)	121	386
– Pension Plan of the Université du Québec (PPUQ)	8 557	3 212
Total for other plans	18 333	77 810
TOTAL	**566 983**	**313 962**

(1) These plans have not accepted any new participants since July 1, 1973.
(2) This plan has not accepted any new participants since it came into effect on January 1, 1992.
Sources: Commission administrative des régimes de retraite et d'assurances (CARRA) and Public Accounts 2011-2012.

❑ Summary description of the retirement plans

The retirement plans of public and parapublic sector employees are defined benefit retirement plans, which means that they provide for a certain level of income for participants upon retirement.

Benefits are calculated on the basis of participants' average income for the best paid years (generally five) and their number of years of service. The pension usually represents 2% of an employee's average income per year of service. Benefits are partially indexed to inflation.

RREGOP and PPMP, which account for nearly 97% of active participants, are cost-sharing plans: the government is responsible for paying 50% of the benefits, and the participants are responsible for paying the other 50%.[1]

Most of the other retirement plans are cost-balance plans. The government covers the cost of these plans, net of contributions paid by participants.

TABLE C.16

Change in the employee contribution rate of certain retirement plans
(per cent)

	RREGOP(1)	PPMP(2)	SPMSQ(3)	PPPOCS(4)
2004	5.35	4.50	8 / 6.2 / 8	4.0
2005	7.06	7.78	8 / 6.2 / 8	4.0
2006	7.06	7.78	8 / 6.2 / 8	4.0
2007	7.06	7.78	8 / 6.2 / 8	4.0
2008	8.19	10.54	8 / 6.2 / 8	4.0
2009	8.19	10.54	8 / 6.2 / 8	4.0
2010	8.19	10.54	8 / 6.2 / 8	4.0
2011	8.69	11.54	8 / 6.2 / 8	4.0
2012	8.94	12.30	8 / 6.2 / 8	4.0
2013	9.18	12.30	8 / 6.2 / 8	6.5

(1) Rate applicable to the excess of 35% of the maximum pensionable earnings (MPE), which is determined by the Régie des rentes du Québec (RRQ). For 2013, the rate applies to the excess of 31% of the MPE. The equivalent rate according to the old formula would be 9.69%. In 2013, the MPE is $51 100.
(2) Rate applicable to the excess of 35% of the MPE.
(3) Rate applicable up to the annual basic exemption of the RRQ ($3 500) / rate applicable to the excess up to the amount of the MPE / rate applicable to the excess of the MPE.
(4) Rate applicable to the excess of 25% of the employee's salary or of the MPE if it is lower.

The Commission administrative des régimes de retraite et d'assurances (CARRA) is responsible for administering the retirement plans.[2]

1 This cost-sharing formula has been in effect since July 1, 1982. Previously, the government was responsible for payment of 7/12 of the benefits.

2 Except for the Pension Plan of the Université du Québec (PPUQ).

❑ Recent changes

To retain qualified workers and delay their retirement, the government has modified RREGOP and PPMP to enable participants to accumulate up to 38 years of service.[3] This change, which was agreed upon during the latest renewal of the collective agreements with government employees, is aimed at ensuring that employees nearing the end of their career stay longer in the labour market, thus facilitating the transfer of expertise.

Bill 58, *An Act to amend the Act respecting the Pension Plan of Management Personnel and other legislative provisions*, was passed by the National Assembly on May 2, 2012. It is the product of consultations with participant representatives and includes several amendments that will foster the financial health of the PPMP. In particular, the pension eligibility criteria have been tightened. Since January 1, 2013, new participants must complete an additional five-year period of membership in the plan for their retirement benefit to be calculated in accordance with the provisions of the PPMP. In addition, the reduction of the benefit for early retirement has been increased.

2.1.1 Retirement plans liability

In its financial statements, the government discloses the present value of the retirement benefits it will pay to its employees, taking into account the conditions governing their plans, as well as their years of service. This value is called the retirement plans liability. It does not take into account the sums accumulated to pay retirement benefits, particularly the Retirement Plans Sinking Fund (RPSF), which will be discussed later on.

The actuarial valuations of the liability of the various retirement plans are carried out by CARRA,[4] following the rules of the Canadian Institute of Actuaries (CIA) and the Canadian Institute of Chartered Accountants (CICA) for the public sector.

In the case of cost-sharing plans (e.g. RREGOP and PPMP), only the portion payable by the government is included in the government liability. In the case of cost-balance plans, the total retirement plans liability is included in the government's liability.

As at March 31, 2013, the liability for the retirement plans of public and parapublic sector employees should stand at $76 573 million. This amount is recognized in the government's gross debt.

3 This measure is being implemented gradually until January 1, 2014.

4 Except in the case of the PPUQ, whose liability valuation is performed by a private-sector actuarial firm.

TABLE C.17

Retirement plans liability
(millions of dollars)

	March 31, 2013[P]
Government and Public Employees Retirement Plan (RREGOP)	45 754
Pension Plan of Management Personnel (PPMP) and Retirement Plan for Senior Officials (RPSO)	10 642
Other plans:	
– Teachers Pension Plan (TPP) and Pension Plan of Certain Teachers (PPCT)	11 545
– Civil Service Superannuation Plan (CSSP)	3 850
– Superannuation Plan of Members of the Sûreté du Québec (SPMSQ)	3 673
– Pension Plan of the Université du Québec (PPUQ)	2 743
– Pension Plan of Peace Officers in Correctional Services (PPPOCS)	842
– Pension Plan of the Judges of the Court of Québec and of Certain Municipal Courts (PPJCQM)	537
– Pension credits under supplemental pension plans	382
– Supplemental pension plan arising from the transfer of the pension plan for non-teaching personnel of the Commission des écoles catholiques de Montréal (SPP of the CECM) to RREGOP	245
– Pension Plan of the Members of the National Assembly (PPMNA)	186
– Pension Plan for Federal Employees Transferred to Employment with the Gouvernement du Québec (PPFEQ)	139
– Supplemental pension plan arising from the transfer of the pension plan for certain employees of the Commission scolaire de la Capitale (SPP of the CSC) to RREGOP	40
– Plan assets(1)	–4 005
Total for other plans	20 177
RETIREMENT PLANS LIABILITY	**76 573**

P: Preliminary results.
(1) Assets of the PPFEQ, SPMSQ, PPUQ, SPP pension credits of the CECM and that of the CSC.

❑ Annual retirement plans expenditure

Every year, the government also records its expenditure as an employer with regard to the retirement plans. This expenditure comprises two components:

- the net cost of vested benefits, that is, the present value of retirement benefits that employees have accumulated for work performed during the year, i.e. $1 808 million in 2012-2013;

- the amortization of revisions to the government's actuarial obligations that result from previous updates of actuarial valuations, for a cost of $605 million in 2012-2013.

In 2012-2013, government spending in respect of the retirement plans should therefore amount to $2 413 million.

TABLE C.18

Spending in respect of the retirement plans
(millions of dollars)

	2012-2013P
Net cost of vested benefits	1 808
Amortization of adjustments arising from actuarial valuations	605
SPENDING IN RESPECT OF THE RETIREMENT PLANS	**2 413**

P: Preliminary results.

In addition, the government must record an interest charge on the obligation relating to the retirement plans from which the investment income of the RPSF is subtracted. This charge is included in debt service.

TABLE C.19

Interest ascribed to the retirement plans
(millions of dollars)

	2012-2013P
Interest on the actuarial obligation(1)	4 988
Less: Investment income of the RPSF	–1 992
INTEREST ASCRIBED TO THE RETIREMENT PLANS	**2 996**

P: Preliminary results.
(1) Net of the income of funds other than the RPSF.

Moreover, in 2012-2013, the government expects to pay $4 802 million to cover its share of the benefits paid to its retired employees. These disbursements do not affect either the government's expenditures or its deficit, because they correspond to expenditures that were already recorded in the past. They are part of the government's non-budgetary transactions.

2.1.2 Retirement Plans Sinking Fund

The Retirement Plans Sinking Fund (RPSF) is an asset that was created in 1993 for the purpose of paying the retirement benefits of public and parapublic sector employees.

As at March 31, 2013, the book value of the RPSF should stand at $48 344 million.

TABLE C.20

Change in the Retirement Plans Sinking Fund (RPSF)
(millions of dollars)

	Book value, beginning of year	Deposits	Investment income imputed	Book value, end of year
1993-1994	—	850	4	854
1994-1995	854	—	–5	849
1995-1996	849	—	74	923
1996-1997	923	—	91	1 014
1997-1998	1 095(1)	—	84	1 179
1998-1999	1 179	944	86	2 209
1999-2000	2 209	2 612	219	5 040
2000-2001	5 040	1 607	412	7 059
2001-2002	7 059	2 535	605	10 199
2002-2003	10 199	900	741	11 840
2003-2004	11 840	1 502	862	14 204
2004-2005	14 204	3 202	927	18 333
2005-2006	18 333	3 000	1 230	22 563
2006-2007	22 437(1)	3 000	1 440	26 877
2007-2008	26 877	3 000	1 887	31 764
2008-2009	31 749(2)	2 100	2 176	36 025
2009-2010	36 025	—	2 175	38 200
2010-2011	38 200	2 000	2 065	42 265
2011-2012	42 265	1 000	2 087	45 352
2012-2013P	45 352	1 000	1 992	48 344

P: Preliminary results.
(1) These amounts take into account restatements arising from the government accounting reforms of 1997-1998 and 2006-2007.
(2) This amount takes into account an adjustment arising from consideration of the expected average remaining service life (EARSL) of participants in the PPMP.

The information on the RPSF shown in the preceding table is based on the government's accounting policies, which are in full compliance with generally accepted accounting principles (GAAP) for Canada's public sector.

The book value of the RPSF as at March 31, 2013 is expected to be higher than its market value. As a result of the accounting policies, the difference between these two items will be fully amortized in the coming years. In addition, the financial impact of gradually amortizing the difference is fully incorporated into the government's financial framework over the entire planning horizon. Subsection 2.4 describes these items in greater detail.

The government's accounting policies apply when the return on the RPSF is higher than anticipated as well as when it is lower. As shown by the following table, the book value of the RPSF has been lower than its market value 8 times in the past 19 years.

TABLE C.21

Book value and market value of the Retirement Plans Sinking Fund as at March 31
(millions of dollars)

	Book value	Market value	Difference
1994-1995	849	831	18
1995-1996	923	954	–31
1996-1997	1 014	1 095	–81
1997-1998	1 179	1 321	–142
1998-1999	2 209	2 356	–147
1999-2000	5 040	5 703	–663
2000-2001	7 059	7 052	7
2001-2002	10 199	9 522	677
2002-2003	11 840	9 240	2 600
2003-2004	14 204	12 886	1 318
2004-2005	18 333	17 362	971
2005-2006	22 563	23 042	–479
2006-2007	26 877	28 859	–1 982
2007-2008	31 764	32 024	–260
2008-2009	36 025	25 535	10 490
2009-2010	38 200	29 559	8 641
2010-2011	42 265	35 427	6 838
2011-2012	45 352	38 222	7 130
2012-2013[P]	48 344	42 023	6 321

P: Preliminary results.

❑ Amounts deposited in the RPSF have no impact on the gross debt

The government issues bonds on financial markets in order to make deposits in the RPSF. Nevertheless, the amounts deposited in the RPSF do not affect the government's gross debt.

Even though the amount of borrowings contracted to make deposits increases the direct debt, these deposits in turn reduce the net retirement plans liability by the same amount. Therefore, the net impact on the gross debt is nil.

TABLE C.22

Illustration of the impact on the government's gross debt of borrowing $1 billion on financial markets in order to deposit it in the RPSF[1]
(millions of dollars)

		Before deposit	After deposit	Change
(A)	Consolidated direct debt	170 625	171 625	1 000
	Retirement plans liability	76 573	76 573	—
	Less: Book value of the RPSF	–48 344	–49 344	–1 000
(B)	Net retirement plans liability	28 229	27 229	–1 000
(C)	Net employee future benefits liability	—	—	—
(D)	Less: Generations Fund	–5 213	–5 213	—
(E)	**GROSS DEBT (E = A + B + C + D)**	**193 641**	**193 641**	—

(1) Illustration based on preliminary results as at March 31, 2013.

❑ A decline in debt service

Deposits in the RPSF entail a reduction in the government's debt service. The rates of return on funds managed by the Caisse de dépôt et placement du Québec (the Caisse) are generally higher than interest rates on Québec government bonds issued to finance deposits to the RPSF. Therefore, the income of the RPSF, which is applied against the government's debt service, is usually higher than the additional interest charges that arise from new borrowings. This leads to a net decrease in the government's debt service.

Since the RPSF was created, the return obtained by the Caisse has been higher than the cost of new borrowings by the government 14 years out of 19.

TABLE C.23

Comparison of the RPSF's annual return and the Québec government's borrowing costs
(per cent)

	Return of the RPSF (1)	Cost of new borrowings (2)	Difference (percentage points)
1994-1995	–3.3 (3)	5.9	–9.2
1995-1996	17.0	5.3	11.7
1996-1997	16.1	6.3	9.8
1997-1998	13.4	5.7	7.7
1998-1999	10.4	5.8	4.6
1999-2000	15.3	7.2	8.1
2000-2001	7.2	6.2	1.0
2001-2002	–4.7	5.5	–10.2
2002-2003	–8.5	4.7	–13.2
2003-2004	14.9	4.6	10.3
2004-2005	11.4	4.4	7.0
2005-2006	13.5	4.4	9.1
2006-2007	13.5	4.4	9.1
2007-2008	5.2	4.8	0.4
2008-2009	–25.6	4.2	–29.8
2009-2010	10.7	4.6	6.1
2010-2011	13.4	4.4	9.0
2011-2012	3.5	4.0	–0.5
2012-2013P	9.4	3.6	5.8

P: Preliminary results.
(1) On a calendar year basis.
(2) On a fiscal year basis.
(3) From February to December 1994.

❑ A flexible deposit policy

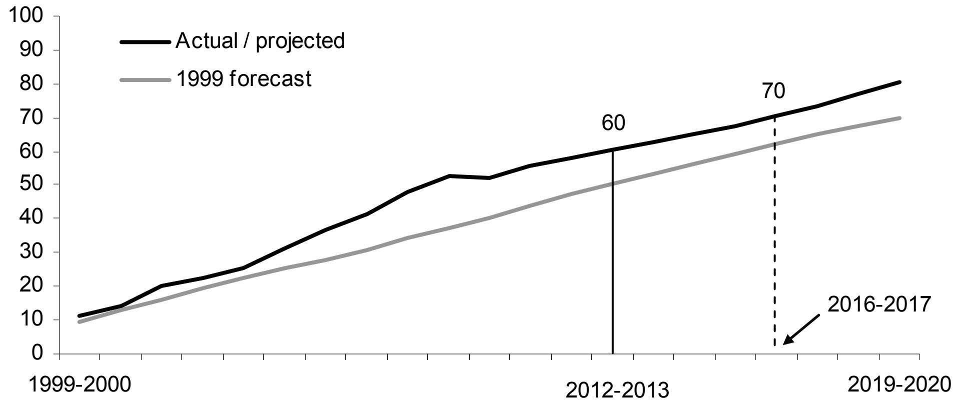
In December 1999, as part of an agreement concluded for the renewal of its employees' collective agreements, the government set the objective that the book value of the funds accumulated in the RPSF would be equal, in 2020, to 70% of its actuarial obligations in regard to the retirement plans of public and parapublic sector employees.

However, the government has all the flexibility needed to apply this policy. Deposits in the RPSF are made only when market conditions are favourable, particularly with respect to interest rates and market receptiveness to bond issues. For example, the government did not make any deposits in 2009-2010, but deposited $2 billion in 2010-2011 and $1 billion in both 2011-2012 and 2012-2013.

The RPSF's book value should represent roughly 60% of the government's actuarial obligations in regard to the retirement plans of public and parapublic sector employees as at March 31, 2013. If deposits of $1 billion per year were made in the RPSF, the target of 70% would be attained three years earlier than anticipated, i.e. in 2016-2017.

CHART C.12

RPSF in proportion to the government's actuarial obligations regarding the retirement plans of public and parapublic sector employees
(per cent)



2.2 Generations Fund

The following table shows the book and market values of the Generations Fund since its creation.

TABLE C.24

Book value and market value of the Generations Fund as at March 31
(millions of dollars)

	Book value	Market value	Difference
2006-2007(1)	584	576	8
2007-2008	1 233	1 147	86
2008-2009	1 952	1 598	354
2009-2010	2 677	2 556	121
2010-2011	3 437	3 524	–87
2011-2012	4 277	4 375	–98
2012-2013P	5 213	5 475	–262

P: Preliminary results.
(1) The first deposit in the Generations Fund was made on January 31, 2007.

Since the first deposit was made in the Generations Fund in January 2007, the return has been higher than or equivalent to the cost of new borrowings by the government five years out of six.

TABLE C.25

Comparison of the Generations Fund's annual return and the Québec government's borrowing costs
(per cent)

	Return of the Generations Fund (1)	Cost of new borrowings (2)	Difference (percentage points)
2007-2008	5.6 (3)	4.8	0.8
2008-2009	–22.4	4.2	–26.6
2009-2010	11.3	4.6	6.7
2010-2011	12.3	4.4	7.9
2011-2012	4.0	4.0	—
2012-2013P	8.4	3.6	4.8

P: Preliminary results.
(1) On a calendar year basis.
(2) On a fiscal year basis.
(3) Return realized from February to December 2007, since the first deposit was made in the Generations Fund on January 31, 2007.

2.3 Returns of the Caisse de dépôt et placement du Québec on funds deposited by the Ministère des Finances et de l'Économie

In 2012, the return on funds deposited by the Ministère des Finances et de l'Économie with the Caisse de dépôt et placement du Québec was 9.39% for the RPSF, 8.35% for the Generations Fund and 8.44% for the Accumulated Sick Leave Fund. The investment policy of these funds is presented in the box on page C.54.

TABLE C.26

Market value and return in 2012 of funds deposited with the Caisse de dépôt et placement du Québec by the Ministère des Finances et de l'Économie

	Return	Market value as at December 31, 2012
	(%)	($ million)
Retirement Plans Sinking Fund	9.39	40 722
Generations Fund	8.35	5 170
Accumulated Sick Leave Fund	8.44	751(1)

(1) This amount reflects the transfer of part of the Accumulated Sick Leave Fund to the Agence du revenu du Québec following the latter's creation.

2.3.1 Retirement Plans Sinking Fund

The RPSF posted a return of 9.39% in 2012. Its market value was $40 722 million as at December 31, 2012.

The assets of the RPSF are managed by the Caisse in accordance with an investment policy established by the Ministère des Finances et de l'Économie in cooperation with the Caisse. This investment policy is established taking several factors into account, including 10-year return, standard deviation and correlation forecasts for various categories of assets, opportunities for investing in these assets and recommendations of the Caisse.

The investment policy of the RPSF consists of 35.75% fixed-income securities (bonds, real estate debt, etc.), 15.50% inflation-sensitive investments (real estate, infrastructure, etc.), 45.25% equities and 3.50% other investments. These weightings are similar to those used on average by the Caisse's depositors as a whole.

TABLE C.27

Investment policy of the RPSF as at January 1, 2013
(per cent)

	Benchmark portfolio of the RPSF	Average benchmark portfolio of depositors as a whole(1)
Fixed-income securities	35.75	35.8
Inflation-sensitive investments	15.50	15.4
Equities	45.25	46.6
Other investments	3.50	2.2
TOTAL	**100.0**	**100.0**

(1) Data as at December 31, 2011. *Annual Report 2011* of the Caisse de dépôt et placement du Québec. The annual report for 2012 was not available as at March 22, 2013.

With its investment policy, the RPSF should generate a short- and medium-term annual return of 6.50%; the average annual long-term (10-year or longer) return is approximately 6.75%. It is important to note that the RPSF's investment policy is based on a long-term horizon and constitutes the benchmark portfolio for the Caisse. However, through active management, the Caisse adjusts the allocation of the RPSF's assets, particularly to take fluctuations in the economic and financial situation into account. The RPSF's benchmark portfolio would have generated a return of 9.21% in 2012.

2.3.2 Generations Fund

The Generations Fund posted a return of 8.35% in 2012. Its market value was $5 170 million as at December 31, 2012.

The assets of the Generations Fund are managed by the Caisse in accordance with an investment policy established by the Ministère des Finances et de l'Économie in cooperation with the Caisse. This investment policy is established taking several factors into account, including 10-year return, standard deviation and correlation forecasts for various categories of assets, opportunities for investing in these assets and recommendations of the Caisse.

The investment policy of the Generations Fund consists of 41.0% fixed-income securities (bonds, real estate debt, etc.), 13.5% inflation-sensitive investments (real estate, infrastructure, etc.), 42.5% equities and 3.0% other investments.

TABLE C.28

Investment policy of the Generations Fund as at January 1, 2013
(per cent)

	Benchmark portfolio of the Generations Fund	Average benchmark portfolio of depositors as a whole(1)
Fixed-income securities	41.0	35.8
Inflation-sensitive investments	13.5	15.4
Equities	42.5	46.6
Other investments	3.0	2.2
TOTAL	**100.0**	**100.0**

(1) Data as at December 31, 2011. *Annual Report 2011* of the Caisse de dépôt et placement du Québec. The annual report for 2012 was not available as at March 22, 2013.

The investment policy of the Generations Fund aims to achieve a long-term (10-year or longer) return of about 6.5%. It is important to note that the investment policy of the Generations Fund is based on a long-term horizon and is the benchmark portfolio for the Caisse. However, through active management, the Caisse adjusts the allocation of the Generations Fund's assets, particularly to take fluctuations in the economic and financial situation into account. The benchmark portfolio of the Generations Fund would have generated a return of 8.88% in 2012.

2.3.3 Accumulated Sick Leave Fund

The Accumulated Sick Leave Fund (ASLF) posted a return of 8.44% in 2012. Its market value was $751 million as at December 31, 2012.

The assets of the ASLF are managed by the Caisse in accordance with an investment policy established by the Ministère des Finances et de l'Économie in cooperation with the Caisse. Since January 1, 2009, the ASLF's investment policy has been identical to that of the RPSF, as the creation of the ASLF stems from a long-term commitment made by the government in regard to employee future benefits, which is similar to the commitment regarding the retirement plans. The ASLF's benchmark portfolio would have generated a return of 9.21% in 2012.

Comparison of investment policies

Investment policies as at January 1, 2013
(per cent)

Specialized portfolios	RPSF and ASLF	Generations Fund	Average benchmark portfolio of depositors as a whole (1)
Short-Term Investments	1.0	1.0	1.2
Bonds	28.75	34.0	26.4
Long-Term Bonds	0.0	0.0	2.3
Real Estate Debt	6.0	6.0	5.9
Total – Fixed Income	**35.75**	**41.0**	**35.8**
Real Return Bonds	0.0	0.0	0.8
Infrastructure	5.0	4.5	3.9
Real Estate	10.5	9.0	10.7
Total – Inflation-Sensitive Investments	**15.5**	**13.5**	**15.4**
Canadian Equity	12.75	10.0	12.9
Global Equity	7.0	8.0	5.8
Québec International	—	—	3.2
Global Quality Equity	1.0	1.0	—
US Equity	5.0	5.5	4.9
Foreign Equity (EAFE)	5.0	5.5	6.1
Emerging Markets Equity	4.5	4.5	3.9
Private Equity	10.0	8.0	9.8
Total – Equity	**45.25**	**42.5**	**46.6**
Hedge Funds	3.5	3.0	2.2
Asset Allocation	0.0	0.0	0.0
Total – Other Investments	**3.5**	**3.0**	**2.2**
TOTAL	**100.0**	**100.0**	**100.0**

RPSF: Retirement Plans Sinking Fund.
ASLF: Accumulated Sick Leave Fund.
EAFE: Europe, Australasia, Far East.
(1) Data as at December 31, 2011. *Annual Report 2011* of the Caisse de dépôt et placement du Québec. The annual report for 2012 was not available as at March 22, 2013.

2.4 Impact of the returns of the Retirement Plans Sinking Fund on debt service

As indicated previously, the income of the RPSF is applied against the government's debt service. The returns of the Caisse affect RPSF income and therefore debt service.

The returns realized by the Caisse on the RPSF are taken into account in the government's balance sheet and results by applying the accounting policy adopted in the wake of the December 2007 reform of government accounting in accordance with generally accepted accounting principles (GAAP).

> When determining a government's retirement benefit liability and expense, plan assets would be valued at market-related values. Under this method, plan assets are recorded at market value or they are adjusted to market value over a period not to exceed five years. Values adjusted to market closely approximate current economic value in a manner that can minimize short-term fluctuations. Market-related values would be used because they are objective and verifiable. Once a basis of valuation is chosen it would be applied consistently. CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS, *CICA Public Sector Accounting Handbook*, Section PS 3250, paragraph .035.

Under the accounting policy, the "adjusted market value" of the RPSF is adjusted every year based on the returns realized on the fund. If, for a given year, the realized return differs from the anticipated long-term return, the difference between the two is spread over five years. All other things being equal, this means that the adjusted market value and the market value will converge over a five-year period. It is important to note that this method is applied when returns are higher than expected as well as when they are lower.[5]

[5] Before the accounting reform of 2007, the value of the RPSF was adjusted only once every three years, that is, when actuarial valuations were carried out. Since the reform, it is adjusted every year.

In addition, the differences between the realized and expected return, which are spread over five years, are taken into account in RPSF income by amortizing them over a period of about 13 years, that is, the expected average remaining service life (EARSL) of retirement plan participants.[6] This amortization mechanism and the period used are prescribed by GAAP.[7]

Therefore, the losses incurred by the Caisse in 2008-2009 reduced the income of the RPSF as of 2009-2010. The returns realized by the Caisse in 2009-2010, which were higher than anticipated, led to an increase in the RPSF's income as of 2010-2011. Similarly, the returns realized by the Caisse in 2010-2011, which were also higher than expected, led to an increase in the RPSF's income as of 2011-2012. In 2011-2012, a rate of return that was lower than the projected long-term rate of return led to a decline in RPSF income as of 2012-2013. Lastly, a rate of return higher than expected in 2012-2013 will increase the RPSF income as of 2013-2014.

TABLE C.29

Impact of the returns of the Caisse de dépôt et placement du Québec on debt service(1)
(millions of dollars)

	2009-2010	2010-2011	2011-2012	2012-2013	2013-2014F	2014-2015F
Before 2008-2009	–48	–78	–57	11	10	16
From 2008-2009	307	629	972	1 337	1 726	1 726
From 2009-2010		–65	–134	–207	–285	–369
From 2010-2011			–53	–110	–171	–236
From 2011-2012				15	30	47
From 2012-2013					–9	–18
IMPACT ON DEBT SERVICE	**259**	**486**	**728**	**1 046**	**1 301**	**1 166**

F: Forecasts.
Note: A positive entry indicates an increase in debt service and a negative entry, a decrease.
(1) The amounts represent the impact on RPSF income, and therefore on debt service, of returns of the Caisse that are lower or higher than the projected rate for that period and that are amortized.

6 As with recognition of the retirement plans liability, the RPSF accounting method draws a distinction between the Pension Plan of Management Personnel (PPMP) and the other plans. The EARSL under the PPMP is 9 years compared with 14 years under the other plans.

7 "…actuarial gains and losses should be amortized to the liability or asset and the related expense in a systematic and rational manner over the expected average remaining service life of the related employee group." CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS, *CICA Public Sector Accounting Handbook*, Section PS 3250, paragraph .062. For the purposes of retirement assets, the CICA defines actuarial gains (losses) as changes in the value of plan assets that are caused notably by variances between actual results and projected results.

APPENDIX 3: INFORMATION RELATING TO CREDIT RATINGS

3.1 The Québec government's credit ratings

A borrower's credit rating measures its capacity to pay the interest on its debt and repay the principal at maturity. To establish the credit rating of a borrower like the Québec government, credit rating agencies analyze a series of economic, fiscal and financial factors. Among the main factors are the size, structure and vitality of the economy, the situation on the labour market, fiscal competitiveness, public finance situation and indebtedness.

To express the quality of a borrower's credit, credit rating agencies use rating scales, namely, a scale for long-term debt and a scale for short-term debt.

The following table shows the rating scales used by agencies for long-term debt. The current credit ratings for Québec are indicated in bold.

TABLE C.30

Credit rating scales for long-term debt

Definition	Moody's	Standard & Poor's	DBRS	Fitch Ratings	Japan Credit Rating Agency
Extremely strong capacity to pay interest and repay principal.	Aaa	AAA	AAA	AAA	AAA
Very strong capacity to pay interest and repay principal.	Aa1	AA+	AA (high)	AA+	**AA+**
	Aa2	AA	AA	AA	AA
	Aa3	AA-	AA (low)	**AA-**	AA-
Strong capacity to pay interest and repay principal, despite greater sensitivity to economic conditions than levels AAA and AA.	A1	**A+**	**A (high)**	A+	A+
	A2	A	A	A	A
	A3	A-	A (low)	A-	A-
Adequate capacity to pay interest and repay principal. Difficult economic conditions may reduce this capacity.	Baa1	BBB+	BBB (high)	BBB+	BBB+
	Baa2	BBB	BBB	BBB	BBB
	Baa3	BBB-	BBB (low)	BBB-	BBB-
Uncertain capacity to pay interest and repay principal, particularly under difficult economic conditions.	Ba1	BB+	BB (high)	BB+	BB+
	Ba2	BB	BB	BB	BB
	Ba3	BB-	BB (low)	BB-	BB-
Very uncertain capacity to pay interest and repay principal, particularly under difficult economic conditions.	B1	B+	B (high)	B+	B+
	B2	B	B	B	B
	B3	B-	B (low)	B-	B-

Agencies add an “outlook” to the rating that indicates the trend the credit rating may follow in the future. The outlook may be positive, stable or negative. In the case of Québec, all of the agencies assign a “stable” outlook to its credit rating.

TABLE C.31

The Québec government’s current credit ratings

Agency	Rating	Outlook
Moody's	Aa2	Stable
Standard & Poor's (S&P)	A+	Stable
Dominion Bond Rating Service (DBRS)	A (high)	Stable
Fitch Ratings (Fitch)	AA-	Stable
Japan Credit Rating Agency (JCR)	AA+	Stable

The following table shows the rating scales used by agencies for short-term debt. The current credit ratings for Québec are indicated in bold.

TABLE C.32

Credit rating scales for short-term debt(1)

Definition	Moody's	Standard & Poor's	DBRS	Fitch Ratings
Very strong capacity to pay interest and repay principal over the short term.	**P-1**	**A-1+** A-1	R-1 High **R-1 Middle** R-1 Low	**F1+** F1
Very adequate capacity to pay interest and repay principal over the short term, despite greater sensitivity to economic conditions than the upper level.	P-2	A-2	R-2 High	F2
Adequate capacity to pay interest and repay principal over the short term. Difficult economic conditions may reduce this capacity.	P-3	A-3	R-2 Middle R-2 Low R-3	F3
Uncertain capacity to pay interest and repay principal over the short term. Securities in this category are considered speculative securities.	Not Prime(2)	B-1 B-2 B-3 C	R-4 R-5	B C
Incapacity to pay interest and repay principal over the short term. Securities in this category are considered default securities.	Not Prime(2)	D	D	D

(1) Not applicable in the case of JCR.
(2) Moody's uses the “Not Prime” category for all securities not included in the upper categories.

❑ Change in Québec's credit ratings

The following charts show the change in the Québec government's credit ratings. The credit ratings for 2013 are those in effect as at March 22, 2013.

CHART C.13

Credit rating assigned to Québec by Moody's

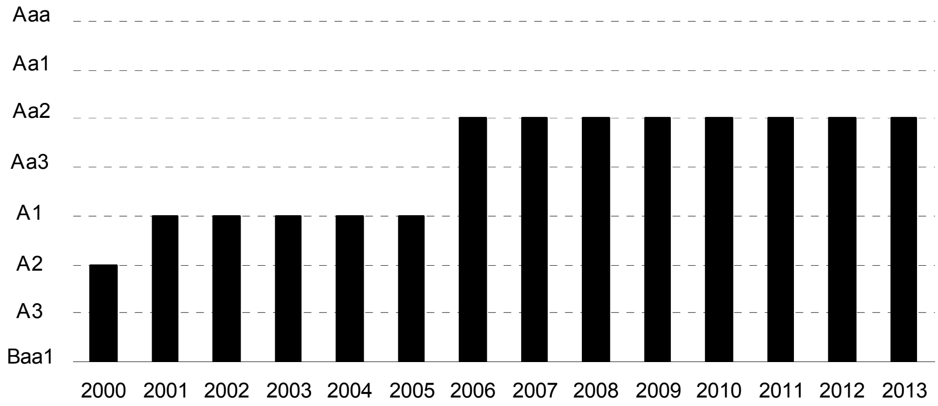


CHART C.14

Credit rating assigned to Québec by Standard & Poor's

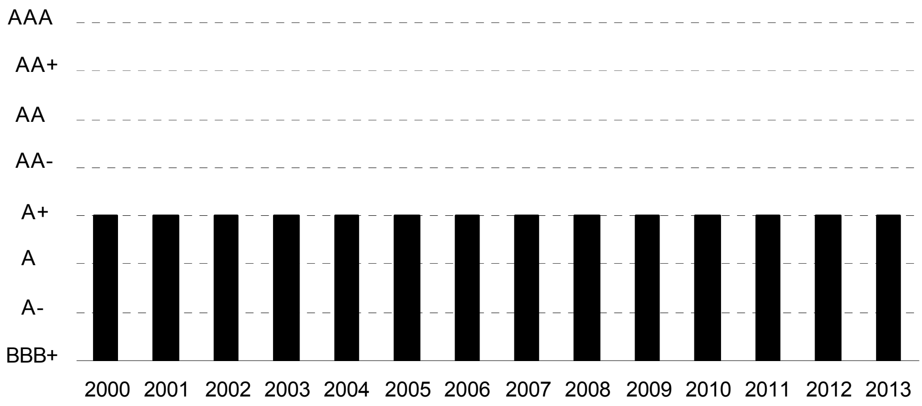
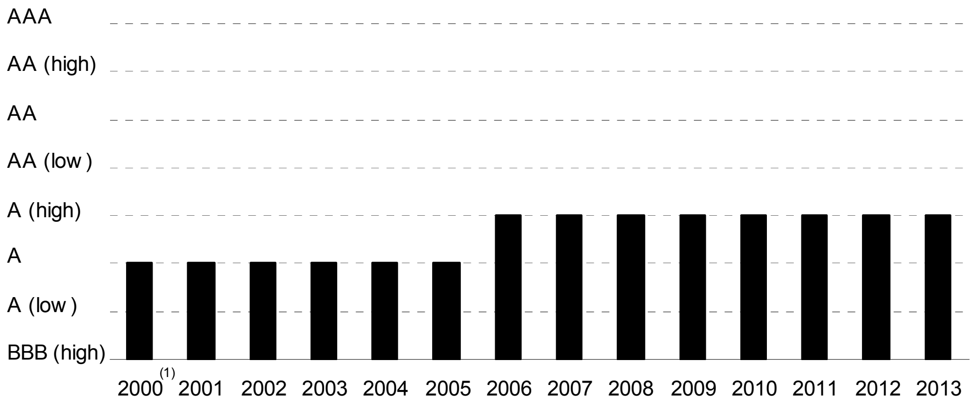


CHART C.15

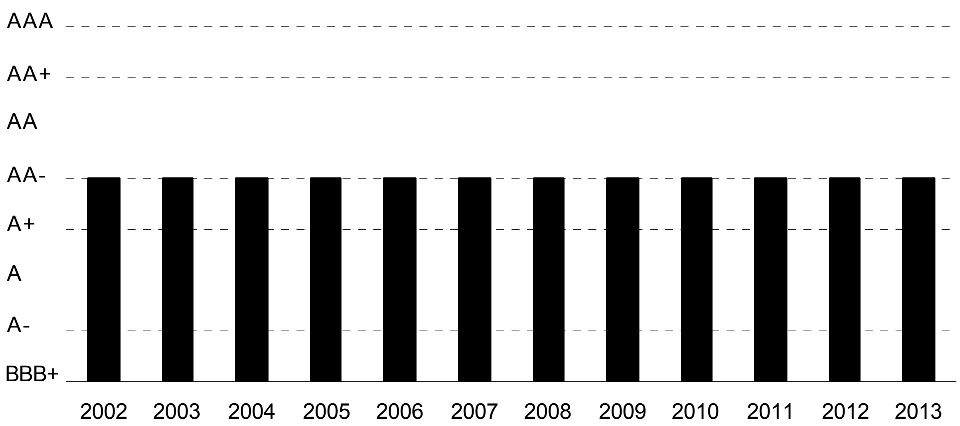
Credit rating assigned to Québec by DBRS



(1) The credit rating was raised from A (low) to A on June 14, 2000.

CHART C.16

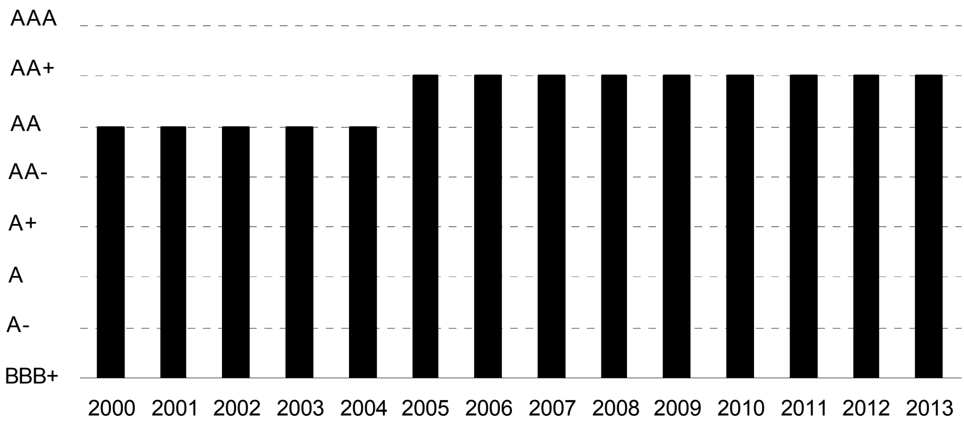
Credit rating assigned to Québec by Fitch



Note: Fitch's credit rating agency has assigned Québec a credit rating since 2002.

CHART C.17

Credit rating assigned to Québec by JCR

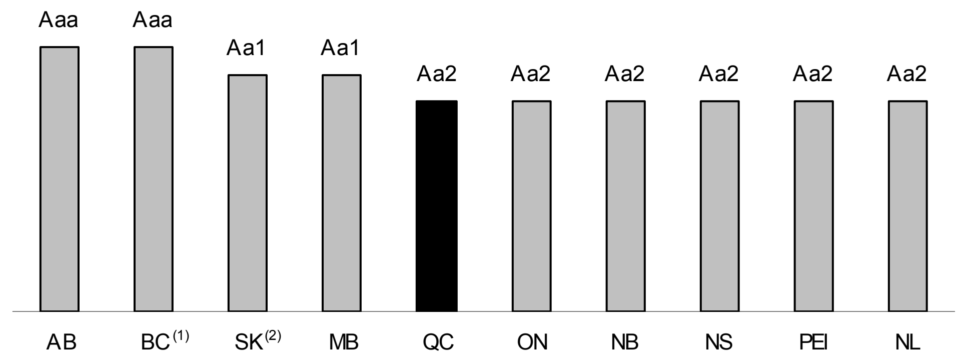


3.2 Comparison of the credit ratings of Canadian provinces

The following charts show the credit ratings of Canadian provinces as at March 22, 2013. No chart is given for JCR since Québec is the only province that receives a credit rating from that agency.

CHART C.18

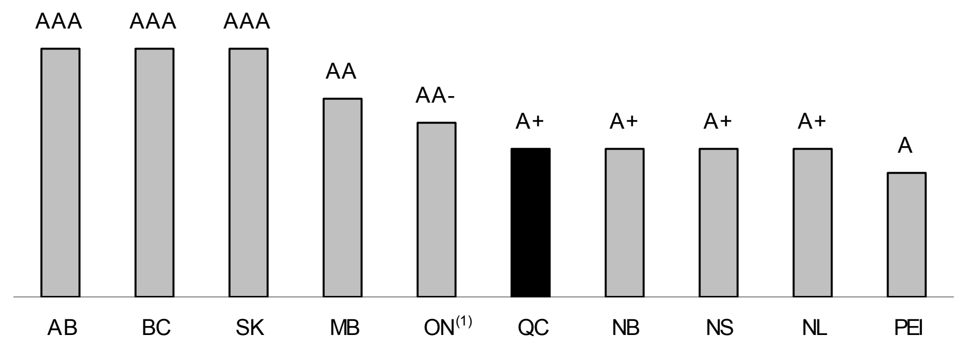
Credit ratings of Canadian provinces ─ Moody's



(1) Negative outlook.
(2) Positive outlook.

CHART C.19

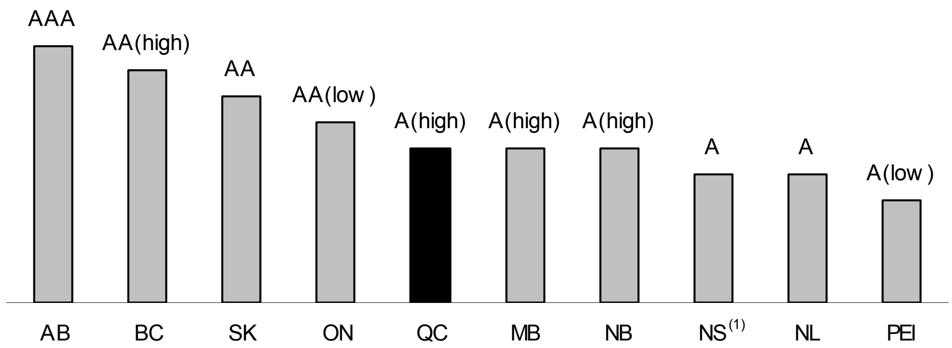
Credit ratings of Canadian provinces ─ Standard & Poor's



(1) Negative outlook.

CHART C.20

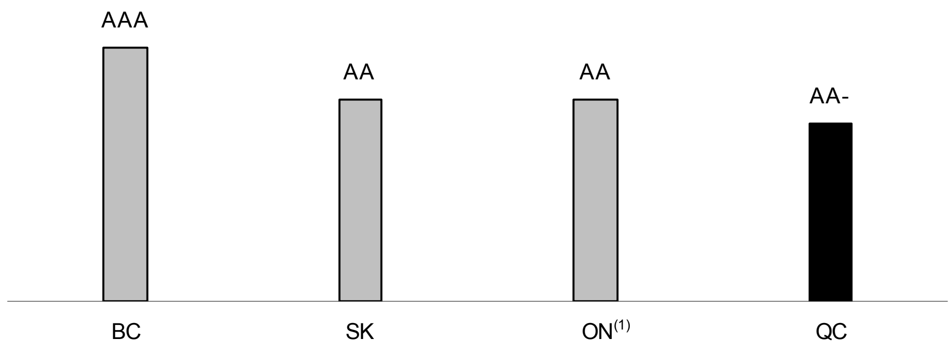
Credit ratings of Canadian provinces ─ DBRS



(1) Positive outlook.

CHART C.21

Credit ratings of Canadian provinces ─ Fitch



Note: British Columbia, Saskatchewan, Ontario and Québec are the only provinces that receive credit ratings from this agency.
(1) Negative outlook.

Section D

IMPLEMENTATION OF THE ECONOMIC VISION

INTRODUCTION **D.3**

1. Funding of higher education **D.5**

1.1 Provide stable long-term funding D.5

1.2 Improved student financial assistance D.8

2. The Banque de développement économique du Québec: Powerful leverage to support investors **D.11**

2.1 Easier access to services and more cohesion in regional economic intervention D.11

2.1.1 Regionalized development fund D.11

2.2 Implementation of the Banque de développement économique du Québec D.11

3. Implementation of economic diversification funds **D.13**

4. A framework for takeover bids of Québec companies **D.15**

5. Bolster research and innovation **D.17**

5.1 Matching funding of $125 million for private-public research partnerships in the biopharmaceutical industry D.17

6. Renewed support for private venture capital funds **D.19**

6.1 Recapitalization of Teralys Capital D.20

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7. Follow-up to the deliberations of the Groupe de travail sur la mode **D.23**

INTRODUCTION

In Budget 2013-2014 last November, the government set out the vision that will guide how it acts on the economy. This vision is based on the certainty that investment is necessary to secure our prosperity. Private investment must now take over from public investments for which major efforts are already underway.

The government's economic vision focuses on private investment as the key to future growth. Indeed, private investment is crucial to improving productivity, the trade balance and the standard of living. Accordingly, the government announced the immediate implementation of several measures to foster private investment, in particular:

— the tax holiday for large investment projects (THI);

— the extension of and improvement to the tax credit for investment in the regions;

— the creation of the Groupe d'action ministérielle pour la mise en œuvre de projets d'investissement privé.

The government's economic vision includes the implementation of many initiatives.[1] The *Update on Québec's Economic and Financial Situation* provides an opportunity to report on certain commitments, including:

— university funding;

— creation of the Banque de développement économique du Québec;

— creation of two economic diversification funds for specific regions;

— a framework for takeover bids of Québec companies;

— enhancement of research and innovation, including the $125 million in matching funding for private-public research partnerships in the biopharmaceutical sector;

— renewed support for two private venture capital funds;

— follow-up to the work of the Groupe de travail sur la mode.

1 MINISTÈRE DES FINANCES ET DE L'ÉCONOMIE, *Budget 2013-2014 – Investing for Our Prosperity: The Government's Economic Vision,* [Paper], November 2012.

1. FUNDING OF HIGHER EDUCATION

1.1 Provide stable long-term funding

❑ Financial commitments for the universities

Following the Sommet sur l'enseignement supérieur last February 25 and 26, the government made important decisions concerning multi-year funding of universities. In particular, it has decided to:

— invest almost $1.8 billion more over seven years in university funding;

— index tuition fees to growth in per capita disposable income to reflect Quebecers' ability to pay.

Accordingly, the government is confirming its commitment to the universities by providing them with stable long-term funding that will reach an annual amount of $3.8 billion in 2018-2019, representing an average annual increase of 4.2% until then.

— The resulting investments will be financed from the spending objectives set for each year of the government's financial framework.

— The amounts from indexing will be added to the funding for universities.

TABLE D.1

Québec government grants to the universities (1)
(millions of dollars)

	2012-2013	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019	Seven-year total
Budget 2013-2014 – Before reinvestment	**2 966**	**3 055**	**3 148**	**3 203**	**3 232**	**3 291**	**3 351**	—
Reinvestment – Sommet sur l'enseignement supérieur								
Reinvestment in university education	10	20	92	157	224	225	226	954
Compensation for the cancellation of the rise in tuition fees(2) of $254 per year	—	—	97	131	163	194	225	810
Subtotal	**10**	**20**	**189**	**288**	**387**	**419**	**451**	**1 764**
QUÉBEC GOVERNMENT GRANTS TO THE UNIVERSITIES AFTER SUMMIT	**2 976**	**3 075**	**3 337**	**3 491**	**3 619**	**3 710**	**3 802**	**—**
Annual % growth		***3.3***	***8.5***	***4.6***	***3.7***	***2.5***	***2.5***	***4.2***

(1) Includes long-term infrastructure funding.
(2) For 2012-2013 and 2013-2014, the compensation is paid from the grants stipulated in Budget 2013-2014.

Government funding for university education

Cumulative reinvestment of almost $1.8 billion

The decisions made at the Sommet sur l’enseignement supérieur have confirmed additional funding for the universities of almost $1.8 billion from now until 2018-2019, including $1.4 billion that will be allocated as follows:

- 75% to achieve national objectives in:
  - quality of teaching, in particular by hiring regular teaching staff,
  - graduation, for instance for first-generation university students, aboriginal students and students from disadvantaged circumstances,
  - training offered in the regions and cooperation among institutions,
  - improved support for research;
- 25% to support institutional philanthropy and adoption of best financial practices and governance.

The balance of the reinvestment, i.e. $405 million, will be added to the base funding of the universities until 2018-2019.

Revision of the university funding policy

Following the summit, the government has embarked on a review of the components of university funding, i.e.:

- funding based on the cost of disciplines;
- funding of short programs, continuing education and distance learning;
- fair contribution from students who are not residents of Québec;
- adjustment of particular envelopes if needed;
- classification of research and of educational and research fields;
- marginal cost and student population recount.

❑ Additional support for the college network

In the course of the recent Sommet sur l'enseignement supérieur, the government announced that it intended to bolster support services for students with special needs in the college network.

Fostering access for all to higher education means that the right to equal opportunity must be upheld. Without special support, some categories of students could in fact be excluded from higher education. Institutions thus have a responsibility to offer services adapted to such students, in particular:

— students with handicaps, of whom there are a growing number attending college. Between 2007 and 2011, their number has grown by 285%, rising from 1 542 to 5 942. They accounted for 3% of college enrolment in 2011 compared with 0.9% in 2007. Almost three quarters of such students have a learning disability, mental health problem or attention deficit disorder, requiring a different approach to support services;

— students from First Nations and Inuit communities, who also have special needs for access to college education and success in their collegiate studies. One of the most effective ways to support these students is to offer them personalized assistance;

— immigrant students, who may need special support because of cultural differences. Implementation of cultural diversity services fosters integration of such students.

Moreover, the government intends to make use of information and communications technologies to boost access to studies and provide quality education.

An additional investment of $5 million a year for the next five years will be allocated for these measures and will be funded from the government's spending objective.

TABLE D.2

Additional investments for the college network
(millions of dollars)

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
Additional investments for the college network	5	5	5	5	5

1.2 Improved student financial assistance

At the Sommet sur l’enseignement supérieur, the government also undertook to improve student financial assistance, in particular by:

- raising the income threshold beyond which the parental contribution is considered in the loans and bursaries plan to $45 000;
- improving the deferred loan payment plan by extending the eligibility period and the period during which one can benefit from the program;
- setting up a mechanism with student associations for working to improve student financial assistance, with annual resources of $25 million.

TABLE D.3

Income threshold beyond which the parental contribution[1] is considered in the loans and bursaries plan
(dollars)

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
New thresholds	36 000	40 000	45 000	45 000	45 000	45 000

(1) For a student whose parents are living together.

The rise in the parental contribution threshold will ultimately benefit some 49 000 students whose financial assistance will increase by $1 350 per year on average.

The cost of these measures will be funded by reducing the rate of the tax credit for tuition and examination fees from 20% to 8% as of the spring of 2013.

TABLEAU D.4

Improved access to studies
(millions of dollars)

	2013-2014	2014-2015	2015-2016-	2016-2017	2017-2018	2018-2019
Tax credits						
Elimination of the non-refundable tax credit for tuition and examination fees(1) at the rate of 20% as of spring 2013	114(2)	156	158	160	162	164
Continuation of the tax credit for the portion of amounts carried forward at the rate of 20%	–54	–46	–39	–34	–29	–25
New non-refundable tax credit at the rate of 8%	–26	–49	–51	–55	–58	–61
Additional revenue from reducing the rate of the tax credit for tuition fees and examination fees from 20% to 8%	**34**	**61**	**68**	**71**	**75**	**78**
Student financial assistance (SFA)						
Increase in the parental contribution threshold	–18	–36	–49	–54	–53	–53
Other SFA improvements under discussion(3)	–16	–25	–25	–25	–25	–25
Subtotal – SFA improvements	**–34**	**–61**	**–74**	**–79**	**–78**	**–78**
Amounts self-financed from the government's spending objective	**—**	**—**	**6**	**8**	**3**	**—**
Subtotal – Additional spending	**–34**	**–61**	**–68**	**–71**	**–75**	**–78**
DIFFERENCE BETWEEN REVENUE AND SPENDING	**—**	**—**	**—**	**—**	**—**	**—**

Note: The effect on the tax credit of indexing tuition fees to per capita household disposable income is included.
(1) The transfer to parents of the unused portion of tuition and examination fees is included.
(2) Impact of $153 million less $39 million for the continuation of the tax credit until the spring of 2013.
(3) Since the year loans and bursaries are granted begins in September of each year, the costs for 2013-2014 are estimated to March 31, 2014, i.e. the end of the government's fiscal year.

2. THE BANQUE DE DÉVELOPPEMENT ÉCONOMIQUE DU QUÉBEC: POWERFUL LEVERAGE TO SUPPORT INVESTORS

2.1 Easier access to services and more cohesion in regional economic intervention

The government will soon table a bill creating the Banque de développement économique du Québec to make state support to investors more coherent and easier for certain client groups to access.

The Bank will consolidate programs previously shared between Investissement Québec and the regional network of the Ministère des Finances et de l'Économie. This will provide Québec with real leverage in favour of private investment that will be operational immediately in every region of Québec.

The Bank will be responsible for front-line intervention in support of business creation and growth. The result will be improved coordination with regional players, local development centres in particular.

For-profit businesses, cooperatives, social economy businesses and foreign investors will have easier access to the full range of services intended for them.

2.1.1 Regionalized development fund

The regionalized development fund results from the consolidation, within the Bank, of the programs currently administered in Québec's regions by Investissement Québec and the Department. It will total at least $500 million annually.

In addition to managing their envelope of the regionalized development fund, the Banks's regional divisions will assist businesses with consulting services as their project moves forward.

In addition, the Bank will manage two funds totaling $250 million that the government has created to assist the regions where asbestos mining and nuclear power generation have ceased.

2.2 Implementation of the Banque de développement économique du Québec

The government's goal is to implement the Banque de développement économique du Québec during fiscal year 2013-2014 to foster the economic development of every region in Québec.

The Bank will report to the Minister for Industrial Policy and the Banque de développement économique du Québec.

3. IMPLEMENTATION OF ECONOMIC DIVERSIFICATION FUNDS

The government has made tough decisions, but necessary ones, to close the Gentilly-2 nuclear power plant and halt the planned re-opening of the Jeffrey mine. For some regions, these decisions mean that it will be necessary to shift their economy to other future-oriented sectors of activity.

In that context, the government announced, as part of Budget 2013-2014, that two economic diversification funds would be set up:

— the first, amounting to $200 million, is intended for the Centre-du-Québec and Mauricie regions;

— the second, with $50 million, is earmarked for the des Sources regional county municipality in the Asbestos region.

The economic diversification fund for the Centre-du-Québec and Mauricie regions and the fund for the des Sources RCM will be the chief instruments for supporting diversification projects in these territories. They will seek to create leverage to support business start-up and development projects, mainly for SMEs, and will foster the growth of new industries.

To guide the government's action in the territories concerned, an economic diversification committee, consisting of the main local socio-economic stakeholders, has been set up for each fund. For their respective territory, the diversification committees have been mandated to initiate a structured diversification process and propose a diversification plan focusing on the strengths of each territory.

The two diversification committees are expected to table reports in the spring of 2013.

The government will shortly unveil an investment policy for each fund stemming from the deliberations of the economic diversification committees. These policies will lay out the terms and conditions for granting financial assistance, the application assessment process and indicators for expected results.

4. A FRAMEWORK FOR TAKEOVER BIDS OF QUÉBEC COMPANIES

To determine whether our legislative framework is adequate for maintaining business development and decision-making centres in Québec, the government will set up a working group on defensive measures regarding hostile takeover bids targeting strategic Québec companies.

This group, consisting of players recognized by the business community, will be mandated to make recommendations to the Minister of Finance and the Economy.

Moreover, the Autorité des marchés financiers, working with securities authorities elsewhere in Canada, is currently holding consultations on the regulatory regime applicable to public takeover bids so that it better responds to current market realities.

5. BOLSTER RESEARCH AND INNOVATION

Research and innovation contribute to the advancement of knowledge and generate spinoffs in every region of Québec. That is why, at last February's Sommet sur l'enseignement supérieur, the government undertook to, in particular:

— hold a national conference on research and innovation in April 2013. This will help formulate the national policy on research and innovation (NPRI), whose launching is planned for June 2013;

— reinvest $26.5 million in 2013-2014 to ensure coordination between the Québec Research and Innovation Strategy and the NPRI. This amount will be allocated among several sectors:

  — $10.3 million for health;

  — $7.0 million for the environment;

  — $1.5 million for social innovation;

  — $7.7 million for strategic technologies;

— earmark for research up to $340 million of the reinvestment in the universities for the period from 2014-2015 to 2018-2019. The guidelines for using these funds will be set out in the upcoming NPRI.

Through these actions, the government is affirming its commitment to this sector. In so doing, it is ensuring that Québec will be a prime location for research and innovation.

5.1 Matching funding of $125 million for private-public research partnerships in the biopharmaceutical industry

In Budget 2013-2014, the government announced $125-million in matching funding over five years to encourage private-public research partnerships in the biopharmaceutical sector.

This funding of $125 million will help support applied research projects in the major niches of advanced research in which Québec has good potential and a critical mass of researchers. Preferred sectors will be cardiometabolic diseases, oncology, infectiology, genomics, personalized medicine, neuroscience and aging.

The government will announce the details of the call for proposals process in the coming weeks. Two calls for proposals are planned, the first to follow the public announcement and the second early in 2014.

6. RENEWED SUPPORT FOR PRIVATE VENTURE CAPITAL FUNDS

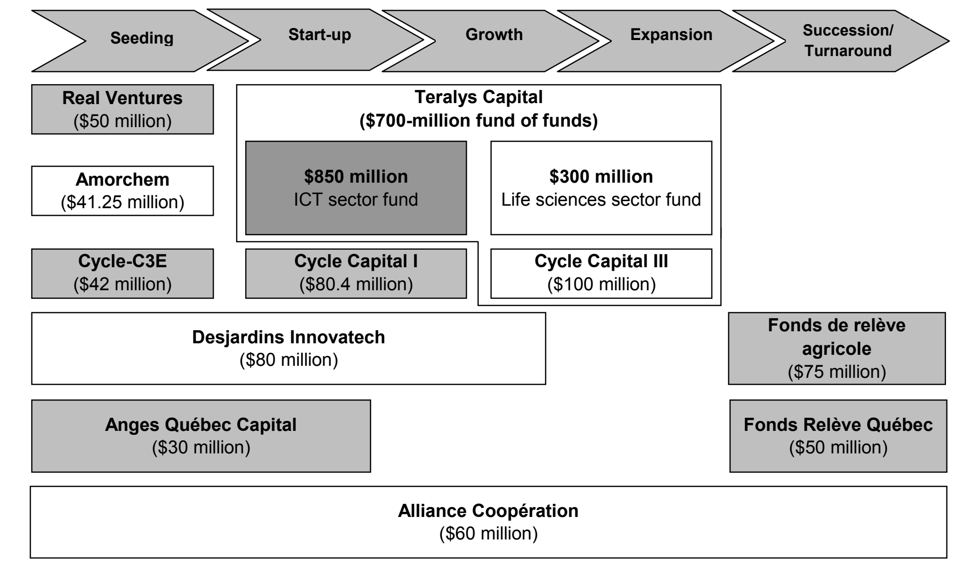
Québec's economic performance relies to a large extent on its capacity to identify and adequately support the best companies so that they can stand out from local and international competition.

That is why the Québec government is making significant efforts to provide an environment conducive to investment and innovation by fostering the development of private venture capital funds that offer financing, but also expertise and business networks.

To achieve its objectives, the Québec government must, among other things, ensure that the most successful funds, whose investment period is nearing its end, are quickly recapitalized to avoid leaving a vacuum in the financing chain and thus allow the most successful companies to continue growing.

Accordingly, the Québec government will ensure that certain initiatives receive appropriate capital to continue investing in sectors where Québec has distinguished itself.

Venture capital funds in which the Québec government has participated according to stage of investment



6.1 Recapitalization of Teralys Capital

After three years, Teralys Capital has invested at a pace consistent with the initial plan, committing almost 60% ($400 million) of its total capital of $700 million. To date, Teralys Capital has set up twelve funds that, with private sector leverage, make $1.25 billion available to support our companies in various activity sectors, namely:

— $850 million in specialty funds in the information technology sector;

— $300 million in specialty funds in the life sciences sector;

— $100 million in a specialty fund in the green technology sector (Cycle Capital III).

By the end of 2013, Teralys Capital is expected to commit to finance about six new funds for total investments of almost $200 million. Creation of these new funds should make an additional $675 million or so available to Québec entrepreneurs.

In this context, the Québec government and its partners in Teralys Capital, namely the Caisse de dépôt et placement du Québec and the Fonds de solidarité FTQ, have agreed to begin working on the recapitalization of Teralys Capital.

6.2 Recapitalization of Anges Québec Capital

Angel investors are key players in the seeding and start-up of businesses. They detect promising projects and contribute to their success by investing capital in them, but also by mentoring new entrepreneurs. Their involvement in the financing ecosystem must be encouraged since private venture capital shows little interest in this stage of investment.

In Québec, the Anges Québec network, with more than 120 private investors, already has a presence in major centres and is active with technology companies. Its objectives are to extend its activities in the regions and broaden its investments to the manufacturing sector and to services.

Anges Québec manages the Anges Québec Capital fund that began operating in May 2012. The fund's first year has been a genuine success. At the current pace of investment, the $20 million in capital invested by the Québec government will be almost fully committed by the summer of 2013.

Accordingly, it is now necessary to plan the implementation of a larger fund that can satisfy the financing needs of Québec companies at the seeding stage in every region of Québec and in various activity sectors.

The government, therefore, intends to support Anges Québec in the recapitalization of Anges Québec Capital. The objective is to help promoters finalize a fund, with a target amount of between $50 million and $75 million, to finance approximately ten projects annually over five years.

7. FOLLOW-UP TO THE DELIBERATIONS OF THE GROUPE DE TRAVAIL SUR LA MODE

As part of Budget 2012-2013, the government announced the creation of the Groupe de travail sur la mode consisting of 14 business leaders. This working group was mandated to assess the industry in terms of what it needs to become more competitive, identify concrete actions to, among other things, enhance synergy among various industry players and develop a modern branding strategy specific to Québec that will be supported by all industry players.

The working group recently completed its report. The chief observation to emerge from its deliberations is that improved synergy among various industry players and those of other creative and innovative sectors could make a positive contribution, in particular thanks to the opportunities generated by pooling resources and means.

The government welcomes the working group's observations and will announce within the next few weeks the steps it intends to take after having reviewed all the recommendations.