September 26, 2017

Nova Scotia's 2017–18 September Budget … Proceeding With Its Four-Year Plan

- **Returning with a second majority mandate last spring,** Nova Scotia's Liberal government is tabling a *Budget* for fiscal 2017–18 (FY18), following its April 2017 *Budget* that was not passed due to the election call.
- **As expected, a string of annual surpluses is outlined from FY18 to FY21** totalling $266 million, just $13 million less than the cumulative black ink outlined in April (top chart).
- **Net debt**, as measured by the Province, ended FY17 $0.1 billion below the April *Budget* estimate, resulting in an actual $121 million decline during the year to $14.95 billion (36.3% of GDP). The September path for net debt is thus $0.1 billion lower, but otherwise unchanged from April. Forecast FY18–FY21 annual increases in net debt average a modest $132½ million. This drops Nova Scotia's net debt below 34% of GDP by March 2021, in sight of the One Nova Scotia goal of 30% by March 2024.
- **Nova Scotia's borrowing plan** also is little changed from April. Forecast FY18 term borrowing of $684 million follows a similarly modest $750 million in FY17. The outlined increase in term borrowing for FY19–FY21 mirrors a surge in debt maturities from $0.5 billion in FY18 to $1.3 billion in FY19 and $2.1 billion the following year, before returning to $1.1 billion in FY21.

OVERVIEW

The September *Budget* reintroduces the government's initiatives from April. Personal income tax relief is targeted towards lower- and moderate-income residents[1] and the threshold for the Province's 3.0% small business income tax rate is lifted.[2] With a larger-than-expected final FY17 balance, this *Budget* injects additional funding for health, education and economic development. The numerous actions in this *Budget* reflect the government's renewed effort to improve life across Nova Scotia, finding more jobs for youth and more opportunities for the middle class.

Revenues in FY18 will be boosted by the $110 million capital contribution from the federal government and the Halifax Regional Municipality towards the new Halifax Convention Centre, recognized this Fall as the Centre reaches substantial completion. As discussed in the past two *Budget* documents, the capital contribution will be directed to future fiscal capacity to continue the QEII Health Sciences Complex redevelopment, leaving a positive FY18 balance of $21 million.

[1] For Personal Income Tax, the Basic Personal Amount plus the Spousal, Age and Dependant Amounts will rise 35.4% as of January 2018 for taxable incomes up to $25,000. The increase will be phased out for taxable incomes from $25,000–$75,000 *(FY19 tax saving: more than $85 million)*.

[2] For the 3% small business corporate income tax rate, the income threshold is increased from $350,000 to $500,000 as of January 2017 (FY18 partial year tax saving: $14 million).

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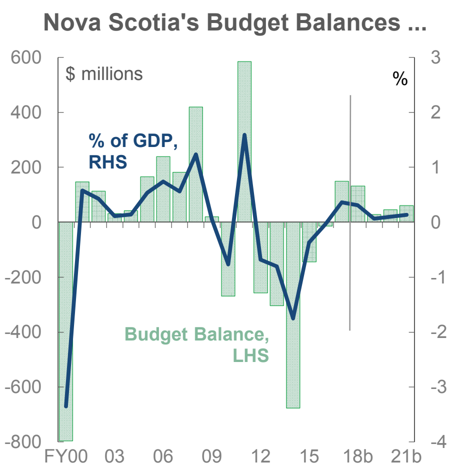
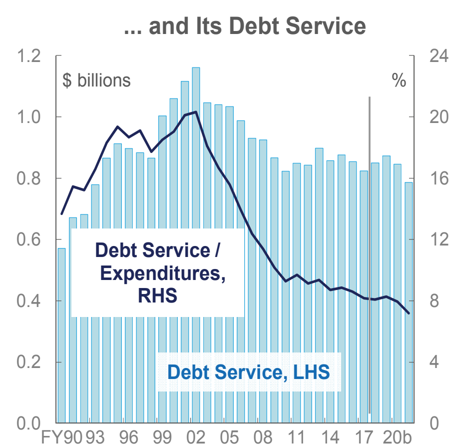




Sources for charts: Nova Scotia Finance; Statistics Canada; nom. GDP forecasts: Scotiabank Economics.

REVENUE DETAILS

Revised *Budget* estimates indicate FY18 revenue growth of 3.6%. However, setting aside the capital contribution, the projected revenue increase is 2.5%, more in line with the 2¾% gain in FY17. Expenditures in FY18 are expected to advance 4.2%, after the restricted 1.4% increase in FY17 to ensure balanced books.

Relative to the April estimates, forecast FY18 revenues are $13 million lower due to softer own-source receipts, but program spending is almost $4 million less (assisted by a lower pension valuation allowance), the debt service is unchanged and the consolidation and accounting adjustments are more than $4½ million larger, trimming the projected FY18 surplus by just $4½ million. Tax revenues this fiscal year are expected to advance by a moderate 2.2%, dampened by the targeted tax relief introduced.

Nova Scotia is weathering diminished offshore royalties given decreased offshore natural gas production and higher decommissioning costs for the Sable Offshore Energy Project. Any additional decommissioning expenses are likely to result in negative Prior Year Adjustments.

The FY18 Equalization increase for Nova Scotia is a modest $17¾ million (+1.0%). The transfer under the Expert Panel formula is almost $46 million ahead of FY16, but it is trimmed by $28 million as the cumulative difference narrows between the Expert Panel formula transfer and the transfer under the Interim approach in place when the *Offshore Accord* was negotiated. This reduction follows six years of additional Equalization payments to Nova Scotia.

In preparing the September *Budget* estimates, the government assumed solid real GDP growth of 1.1% in calendar 2017, slightly below the average of private-sector forecasts published in late June. Significant job creation to date in 2017 is expected to offer some extra revenue support. For 2018, the government assumes a slowdown in Nova Scotia's growth to 0.5%, more cautious than the private-sector average.

With the assumption that Nova Scotia's nominal GDP growth will slip from 3.2% in 2017 to 2.4% in 2018, FY19 revenues are expected to climb just 0.6% above FY18 receipts after the capital contribution is removed. To retain black ink, the September estimates build in virtually no increase in FY19 program spending. Over the following two years, revenue growth is expected to firm to 2.9% in FY21.

Nova Scotia's Budget Arithmetic
$ millions except where noted

	FY17	FY18 Budget	
	Final	April	Sept.
Personal Income Tax (PIT)	2,637	2,738	2,711
Corporate Income Tax (CIT)	513	506	507
Harmonized Sales Tax (HST)	1,779	1,804	1,829
Other Tax	646	660	647
Total Tax Revenue	**5,574**	**5,709**	**5,694**
Royalties - Petroleum	10	12	12
Gov.Bus.Enterprises - Net Income	395	379	379
Other Own-Source Revenue	1,519	1,601	1,590
Total Own-Source Revenue	**6,851**	**7,041**	**7,027**
Equalization (+Best-of Guarantee*)	1,733	1,751	1,751
Offshore Offset Accord	33	20	20
Crown Share	2	3	3
Federal Transfers	**3,357**	**3,546**	**3,546**
Total Revenue	**10,208**	**10,587**	**10,574**
Program Spending	9,263	9,666	9,662
Debt Service	824	850	850
Total Expenditures	**10,086**	**10,516**	**10,512**
Consolidation & Adjustments	28	66	70
Provincial Balance	**150**	**136.2**	**132**
Fiscal Capacity,Health Complex: Contrib.	0	110	110
Net Position	**150**	**26**	**21**
Term Debt Requirement	**750**	**620**	**684**
of which: Debt Maturities	997	460	460
Memo Items, %			
Tax Revenue / GDP	13.5	13.4	13.4
Own-Source Revenue / GDP	16.6	16.5	16.5
Program Spending / GDP	22.5	22.7	22.7
Budget Balance / GDP	0.4	0.3	0.3
Debt Service / Revenue	8.1	8.0	8.0
Annual Change, %			
Total Tax Revenue	*2.8*	*2.4*	*2.2*
Personal Income Tax (PIT)	*2.9*	*3.9*	*2.8*
Corporate Income Tax (CIT)	*11.1*	*-1.4*	*-1.2*
Harmonized Sales Tax (HST)	*1.0*	*1.4*	*2.9*
Own-Source Revenue	***3.3***	***2.8***	***2.6***
Federal Transfers	*1.6*	*5.6*	*5.6*
Total Revenue	***2.8***	***3.7***	***3.6***
Program Spending	*1.9*	*4.4*	*4.3*
Total Expenditures	***1.4***	***4.3***	***4.2***

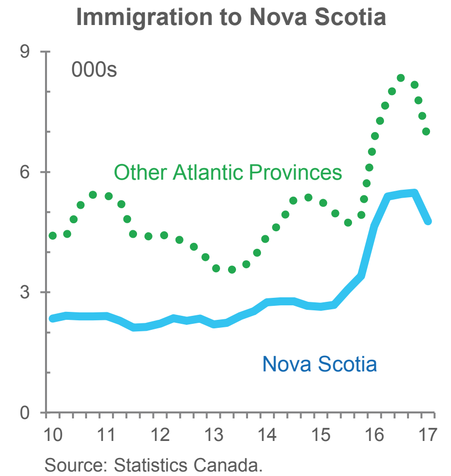
*For FY09-FY20, Equalization under the Expert Panel formula plus any cumulative shortfall vs the Interim formula in place at the time of the *Offshore Accord*.

Source: Nova Scotia Finance; Statistics Canada; nom.GDP fcsts: Scotiabank Economics.

EXPENDITURE DETAILS

Constrained by revenue growth, the program spending path is uneven in this four-year fiscal plan. The government's second term begins with a 4.4% program spending surge in FY18, but further significant advances are limited to the 2.5% average annual gains in FY20 and FY21. Assisting the eventual uptick in program spending is the declining share of total expenditures required for the debt service (bottom chart, p.1). In contrast to a number of Provinces facing increasing interest charges in the rising interest rate environment anticipated over the next few years, Nova Scotia expects its debt service to stabilize in the $850 million range from FY18 to FY20, absorbing an average 8.1¢ of each revenue dollar. In FY21, interest costs are expected to decline to $786 million, opening up new room for program spending.

In response to public demand, Health and Wellness outlays are slated to expand 2.7% with measures such as: enhancing primary care through collaborative teams; training additional doctors and recruiting more health professionals; introducing an affordable take-home therapies program for cancer patients; and accelerating mental health care. **In Education**, a priority is rolling out pre-primary full-day programs for four-year olds to assist their learning and, importantly, to reduce daycare costs for families.



Critical in sustaining balanced books is economic growth. In its first term, the government restructured Nova Scotia's economic development efforts, scaling back the provision of direct subsidies to individual firms and instead strengthening the province's competitiveness by focusing on many of the One Nova Scotia goals emerging from the 2014 *Ivany Report.* Measures range from multi-year development support for aquaculture and vineyards/wineries to encouraging work force development. With respect to skilled trades, tuition will be eliminated for apprentices' technical training and seven new Skilled Trades Centres will be opened in schools. Retaining a larger share of Nova Scotia's college and university graduates in the province has been a longstanding objective, and a new focus is incorporating Masters and PhD students more quickly into the economy. Nova Scotia has been successful in attracting more international immigrants (top chart), looking to their skills and entrepreneurial talent, in part due to the *Atlantic Immigration Pilot,* partnered between the federal government and the four Atlantic Provinces. To grow exports, initiatives include a new export accelerator program and upgrades to the Province's key tourism sites, taking advantage of a competitive Canadian dollar vis-à-vis the US dollar.

With respect to both operating and capital expenditures, difficult issues persist, such as the government's decision this summer to avoid third-party independent arbitration boards in settling extended labour negotiations.[3] Ongoing efficiencies include the government's use of its discretionary sinking funds, totalling $876½ million as of March 2017, to manage its debt maturities and debt issuance.

OUTLOOK

On a range of initiatives, such as red tape reduction, the Province's success has prompted more ambitious performance goals. To stay on plan, the *Speech from the Throne* referenced the creation of an Office of Strategy Management to ensure collaborative development and the communication and measurement of the government's priorities. In expanding its social program commitments, the government raises the stakes on continued expenditure management as Nova Scotia's economic growth moderates towards the end of the decade. Though this *Budget* focuses on youth employment, opportunities for the middle class and assisting the less fortunate, sustaining these programs relies upon the government's commitment to further build Nova Scotia's fiscal flexibility.

[3] See Fiscal Pulse, p 2, September 2017, here.