New Brunswick: 2017–18 Q3 Update

ECONOMIC GROWTH HELPS TO FURTHER NARROW THE DEFICIT

The Q3 *Update* positions New Brunswick to enter fiscal 2018-19 (FY19) with greater-than-anticipated progress on fiscal repair.

- As of Q3, a $115 million deficit (-0.3% of GDP) is forecast for FY18, representing a hefty $77 million improvement on the *Budget* deficit estimate and the second consecutive year of modest red ink.
- Net debt, as measured by New Brunswick, is now expected to rise by just $273 million during FY18, dropping towards 40% of GDP by year-end.
- The Province is working through several issues, including the development of a "made-in-New Brunswick" carbon pricing plan (text box, p. 2-3).

REVENUE AND EXPENDITURE DETAILS

New Brunswick's FY18 Q3 *Update* (here) reflects an in-year $74 million revenue gain supplemented by an $18 million saving on the debt service that more than covers program spending running $15½ million above *Budget* (table, p.2).

Revised FY18 revenue growth of 4.2% is driven by a 6.5% surge in tax receipts. Escalating corporate income tax (CIT) and HST receipts mirror positive federal tax base and prior-year CIT adjustments. The buoyancy in tax receipts also reflects firmer resource prices and New Brunswick's healthy economic expansion, including a rebound in retail sales (side chart). In the Q3 *Update,* the government raised its forecast of 2017 real GDP growth to 1.3% from its 0.8% Q2 estimate. Yet similar to other Provinces, New Brunswick reports an unexpected 2.2% drop in FY18 personal income tax (PIT) revenues as the 2016 tax assessment information is incorporated that quantifies high-income individuals' tax planning in advance of Ottawa's new top PIT bracket as of 2016.

Government enterprise net income is soft this year. Though NB Power reduced its debt during the first half of FY18, its operating earnings for the six months were $27 million less than a year earlier and $22 million below *Budget,* with low water levels hampering hydro-electric power generation. A 1.77% average power rate increase across all customer classes was implemented on April 1, 2017. Slow, steady rate increases are part of NB Power's longer-term strategy to pay down debt and prepare for large capital projects such as the life -cycle extension of the Mactaquac hydro-electric dam.

The projected 4.3% program spending expansion for FY18 stems from ongoing Health and Social Development expense pressures plus specific items such as the costs related to the 2017 ice storm. Yet several one-time events also benefitted New Brunswick, such as the sizeable debt service saving from historically low rates and refinancing a capital lease.

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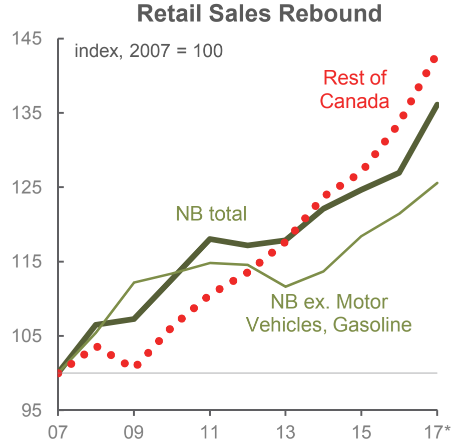


* Jan. - Nov. Source: Statistics Canada.

With respect to planned expenditure savings, the government, as in prior quarters, reports shortfalls largely resulting from specific events such as several large unions not accepting the elimination of their Retirement Allowance in exchange for higher wages and the additional teachers required to accommodate the Syrian refugees.

POLICY DEVELOPMENTS

The *New Brunswick Capital Markets Report* for 2017 indicates that $1.45 billion was raised by NB's public and private companies. Encouraging for the government as it further develops an innovation strategy is the trend in venture capital investments towards later-stage development companies, with the majority of deals in the information and communications technology industry.

Three out of four NB universities have agreed to the Province's four-year framework that provides them with operational funding increases of 1% annually for the first three years and 2% for 2020-21. In exchange, tuition fee increases for a degree are capped to 2% annually for students enrolled in 2018-19 or earlier. Pilot projects are proceeding to bolster enrolment and broaden research & development opportunities. The Province is proceeding with its free tuition program for low-income students and reduced tuitions for students from middle class families.

New Brunswick's Budget Arithmetic

$ millions except where noted

	FY17	FY18	
	Final	**Budget**	**Q3**
Personal Income Tax	1,642	1,681	1,605
Corporate Income Tax	328	334	437
Harmonized Sales Tax	1,254	1,419	1,450
Metallic Minerals Tax	1	1	3
Other Taxes	1,066	1,084	1,076
Total Taxes	**4,291**	**4,519**	**4,571**
Resource Royalties	80	70	74
Other Revenues	4,519	4,599	4,618
Total Revenue	**8,890**	**9,189**	**9,263**
Program Spending	8,336	8,680	8,695
Debt Service*	673	701	683
Total Expenditure	**9,009**	**9,381**	**9,378**
Budget Balance	**-119**	**-192**	**-115**
Memo Items, %			
Program Spending / GDP	24.4	24.6	24.7
Budget Balance / GDP	-0.3	-0.5	-0.3
Debt Service*/ Revenue	7.6	7.6	7.4
Annual Change, %			
Personal Income Tax	*-0.8*	*2.4*	*-2.2*
Corporate Income Tax	*45.4*	*1.9*	*33.2*
Harmonized Sales Tax	*10.3*	*13.1*	*15.6*
Total Taxes	*6.5*	*5.3*	*6.5*
Total Revenue	***6.0***	***3.4***	***4.2***
Program Spending	*4.6*	*4.1*	*4.3*
Total Expenditure	***4.2***	***4.1***	***4.1***

* Excluding government enterprises' debt service. Source: NB Finance; Statistics Canada; nominal GDP forecasts: Scotiabank Economics.

Update on New Brunswick's Climate Change Actions

New Brunswick's *Climate Change Act* follows its December 2016 Action Plan, *Transitioning to a Low-Carbon Economy.* It is the Province's response to the federal requirement for a price on carbon that climbs from $10/tonne of carbon dioxide equivalent (CO_2e) in 2018 to $50 by 2022 that also aims to safeguard its residents, particularly low-income families, and its business sector, especially those firms that are energy intensive and trade-exposed.

New Brunswick maintains that it has already achieved the federal 2030 target of cutting GHG emissions 30% below 2005 levels. Accomplishing a 35% decrease by 2030 would require additional measures that the Province supports if they are undertaken at the lowest "net cost" possible.

The four pillars of NB's "modified hybrid carbon pricing system" are summarized below to highlight the variation emerging across provincial carbon price strategies and the inevitable future debates on the efficiency and effectiveness of different approaches.

1. Diverting a portion of NB's existing gasoline and motive fuel taxes to climate change initiatives

- To avoid adding to consumers' tax burden with either a carbon tax or a cap-and-trade framework, NB argues that its residents are paying an implicit price on carbon via the two provincial fuel taxes that is greater than Alberta's total provincial taxation on gasoline and motive fuel, even with a $50 carbon price.

Update on New Brunswick's Climate Change Actions *(continued)*

- This year, 2.33¢/litre of NB's total 15.5¢ gasoline tax and 2.76¢/litre of its 21.5¢ motive fuel tax will be directed to a *Climate Change Fund* and deployed for emissions mitigation or climate change adaptation. This revenue reprofiling will rise by equal amounts in each of the four following years to 11.64¢/litre of the gasoline tax in 2022 and 13.8¢ of the motive fuel tax. The fuel tax allocation to the *Fund* steadily rises from $37 million in the first year (total revenue from the two taxes is $286 million) to an estimated $180 million.

2. Placing NB's large industrial emitters under the federally administered output-based carbon levy

- For large industrial facilities emitting more than 50,000 tons of CO_2e, a carbon pollution price will only be levied on the emissions exceeding the best practice level (top quartile or higher) for that industry and the entity's production volume. A facility emitting less than the applicable emissions standard will earn surplus credits to be banked for the future or sold to other firms. On emissions over the standard, a carbon price would be charged, or surplus credits or offset credits would be required.

- For New Brunswick, facilities likely subject to this program include several large pulp & paper mills, the oil refinery, the LNG terminal, thermal power generating stations and metals smelting. Several NB entities are currently concerned about the consequences of a national emissions intensity standard rather than a local calculation.

- For the New Brunswick government, relying on the *Federal Carbon Pricing Backstop* for this section of their climate change program represents a considerable saving on the development and administration costs that would be required for a small province to run its own program.

3. Stepping up energy efficiency programs

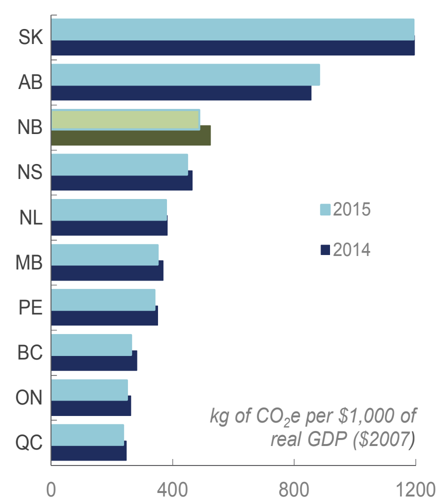
- New Brunswick has announced a five-year $234 million suite of energy efficiency programs for homes, businesses and public buildings. Funding includes up to $51 million from the federal *Low Carbon Economy Fund,* up to $82 million from NB Power over the next three years divided between residential and non-residential projects and $101 million from the Province for energy retrofits and renewable energy upgrades for buildings in the broader public sector.

4. Eliminating coal-fired electricity generation

- The four provinces with coal-fired power generation — Saskatchewan, Alberta, New Brunswick and Nova Scotia — face the federal regulation to close these stations by 2030 (bottom chart). NB is prepared to close its coal-fired plant at Belledune by 2030 if the local economic consequences and the energy cost impacts can be minimized. Otherwise, the Province may opt to extend the phase-out of its coal-fired power generation to 2040 if an equivalency agreement can be reached with the federal government.

- A challenge is NB's commitment to maintaining power generation at Belledune, spurring exploration of the cost and feasibility of converting to other fuels such as biomass, natural gas and hydrogen. Currently $7 million is allocated to assessing a new hydrogen power technology which uses water. Another NB power station eventually requiring reassessment is Coleson Cove that currently burns lower grade bunker oil. For New Brunswick, an aggressive 75% target for clean, renewable or non-emitting power generation depends upon the Point Lepreau nuclear station operating at or close to full capacity to supply just over 40% of the Province's power needs.

GHG Emissions Intensity



Source: Environment Canada.