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# Fiscal Pulse

## Nova Scotia's 2009-10 Fall Budget — Steering Through the Downturn

*With a \$592 million deficit forecast for fiscal 2009-10 (FY10), the new administration is easing the Province's ambitious debt reduction policies, recognizing, like most other Canadian governments, that reversing recent fiscal repair is likely necessary to assure an economic recovery.*

*For FY11 through FY13, balanced books are planned. Yet with revenues forecast to climb only 0.5% in FY11 and just 5.2% over the following two years, a comprehensive review of spending and revenue options will begin shortly.*

*Boosted by accelerated infrastructure investment, the FY10 borrowing program is expected to total \$1.97 billion, up from \$1.48 billion in FY09. Annual financing requirements are expected to average \$1.66 billion for FY11 and FY12, before falling back to \$0.7 billion in FY13. The debt service is forecast to climb 28% from \$867 million in FY09 to \$1.1 billion in FY13, an increase from 10.2¢ of each revenue dollar to 12.5¢.*

**While the Nova Scotia economy has proven relatively resilient**, the economic downturn has weakened revenues more than the previous government's *Budget* in May assumed, and the new administration is proceeding with most of the previously proposed stimulative infrastructure investment and supportive tax relief. Total revenues, after edging 0.3% lower in FY09, are expected to fall a further 1.0% this year, dragged down by a 7.6% correction in Nova Scotia's own-source receipts.

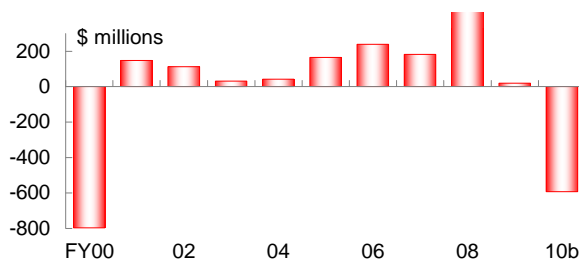
**Tax revenues are expected to slide 0.9% this year**, with Harmonized Sales Tax (HST) receipts just 0.6% higher and personal income taxes in FY10 dropping back to FY08 levels. Corporate income tax (CIT) receipts are forecast to fall 17% below FY08, eroded by carry-back losses and a decline in offshore CIT. Petroleum royalties in FY10 are projected to be one-third the FY09 level, largely because of weak natural gas prices, and to a lesser extent the production losses and expense related to maintenance and the capital cost of a new well in 2009.

**Federal transfers** will offer welcome support, with an anticipated 11½% gain in FY10, elevated by Ottawa's stimulus programs. Nova Scotia is benefitting from its extensive negotiations with Ottawa in recent years. It will receive a one-time transitional payment this year to ensure its Equalization payments in FY10 remain equal to the \$1.465 billion received in FY09. As well, until FY20, Nova Scotia will receive an additional payment from Ottawa if the cumulative value of the Equalization formula in effect when the *2005 Offshore Accord* was signed exceeds the cumulative value of the more recent Expert Panel calculation for Equalization.

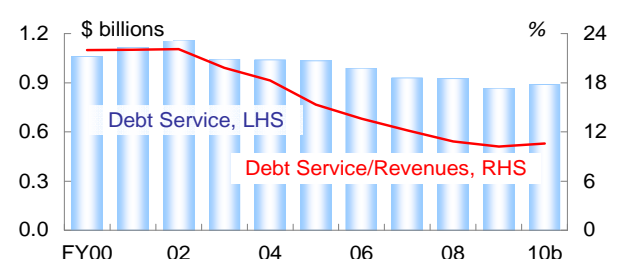
**Since its election in early June**, the new administration has introduced promised measures to make life more affordable for Nova Scotia residents, accomplished through savings in existing budgets. Initiatives include removing the 8% provincial portion of the Harmonized Sales Tax (HST) from basic home electricity as of October 1, and a partial provincial HST rebate on up to 1,500 new homes (see text box, p. 3-4).

**Much of this Budget reflects the prior government's Budget** in May, with many FY10 expenditures already in place and previously slated tax cuts proceeding, such as personal income tax relief this year and

Red Ink Surges in FY10 ...



... But Debt Service Benefits from Low Interest Rates





next. The \$796 million FY10 capital budget covers almost all of the prior infrastructure projects, taking advantage of Ottawa's stimulus to raise federal infrastructure funds for Nova Scotia to \$137 million in FY10, more than double the FY09 level.

**Program spending in FY10 is expected to climb 7.2%.** In addition to several election commitments, selected program reinforcements include HINI preparations, funding a higher-than-expected take-up of home energy-efficiency programs and a \$13 million addition to the Industrial Expansion Fund alongside measures to raise the Fund's accountability. The government has laid out an active agenda. Its promises include a five-year capital plan, a comprehensive renewable energy strategy, a natural resources strategy covering forests, minerals, parks and biodiversity, an immigration policy with enhanced integration efforts and a redesign of the Employment Support and Income Assistance Program.

**Until FY09, Nova Scotia's ambitious debt reduction framework rested on several pillars:**

- ❑ Annual surpluses must be large enough to avoid a rise in debt from tangible asset acquisition or other expenses;
- ❑ To avoid reborrowing the \$830 million debt repayment in 2005 that was accomplished using the upfront payment under the *2005 Accord*, Offshore Offset payments must be excluded from general revenues in calculating the budget balance;
- ❑ A deficit must be recovered in the following year; and,
- ❑ Crown Share payments after FY08 should go to debt retirement.

**Even in FY09, this framework proved too demanding.** The \$20 million FY09 surplus did not cover the \$106 million of Offshore Offset receipts, resulting in a \$84 million deficit under the *Provincial Finance Act*. Planning for an FY10 surplus large enough to offset the FY09 shortfall was not feasible. As highlighted by the government's independent financial review this summer, excluding several one-time gains, growth in Nova Scotia's revenue has been trending lower as its program costs

shift higher given prior commitments, inflation and an aging population. Even windfall receipts from exploration license forfeitures are expected to be subdued, as in FY09, with few licenses close to expiration in the near term and provincial regulation changes to spur new activity making it easier for firms to extend or combine their licenses. Consequently, the government is proceeding with legislative amendments that will accommodate the FY10 deficit and the use of Offshore Offset and Crown Share payments for programs and services. By FY12, Nova Scotia will likely reborrow over \$600 million of its \$830 million debt repayment in 2005 from the *2005 Accord* monies.

**In FY11, a specific challenge** is the anticipated drop of about \$200 million in Nova Scotia's Equalization transfer given the removal of the FY10 transition payment; the current program cap for Equalization growth set at three-year average national GDP gains; and the revised calculation of "fiscal capacity" to the average fiscal capacity of the Equalization-receiving Provinces if Ontario's shift to "have-not" status persists beyond FY10. In FY12 and FY13, the recovery in Nova Scotia's Equalization transfers could well be gradual. Thus, after the prior administration pre-paid a substantial share of the funding assistance for universities for FY10 at the end of FY09, this *Budget* provides an additional \$341 million of university assistance funding in FY10. This will satisfy the funding requirements under the Memorandum of Understanding to the spring of 2011, alleviating some of the spending pressure for FY11. Not until FY12 will regular annual assistance payments for universities likely resume, and by then provincial revenue growth should be slightly stronger.

**Even with this timing adjustment,** the weak 0.5% rebound projected for total revenues in FY11 will force considerable restraint, with the goal of balanced books demanding an 8.1% (\$665 million) decline in FY11 program expenditures, returning these outlays to less than FY09 levels. The government already has embarked on expenditure control with measures such

**Nova Scotia's Budget Arithmetic**  
Consolidated Fund Basis  
\$ millions except where noted

	FY09		FY10
	Budget	Actual	Budget
<b>Own-Source Revenues</b>	<b>5,549</b>	<b>5,548</b>	<b>5,127</b>
Tax Revenue	3,781	3,737	3,701
Royalties - Petroleum	514	452	151
Offshore Licenses Forfeitures	0	2	0
Gov.Bus.Enterprises - Net Income	358	360	357
Other Own-Source Revenue	897	997	917
<b>Federal Transfers</b>	<b>2,916</b>	<b>2,947</b>	<b>3,285</b>
Offshore Accord Payments	106	106	180
Crown Share Adjustment Payment	0	95	79
<b>Total Revenue</b>	<b>8,466</b>	<b>8,494</b>	<b>8,412</b>
Program Spending	7,428	7,654	8,205
Debt Service	905	867	889
<b>Total Spending</b>	<b>8,333</b>	<b>8,521</b>	<b>9,094</b>
<b>Consolidation &amp; Adjustments*</b>	57	46	90
<b>Budget Balance</b>	<b>190</b>	<b>20</b>	<b>-592</b>
<b>Borrowing Requirement</b>	<b>915</b>	<b>1,484</b>	<b>1,968</b>
<b>Memo Items, %</b>			
Own-Source Revenue / GDP	16.2	16.2	15.3
Tax Revenue / GDP	11.1	10.9	11.0
Program Spending / GDP	21.7	22.4	24.4
Debt Service / Revenue	10.7	10.2	10.6
<b>Annual Change, %</b>			
Tax Revenue	3.9	2.7	-0.9
Total Own-Source Revenue	0.9	0.9	-7.6
Federal Transfers	-3.5	-2.5	11.5
Total Revenue	-0.7	-0.3	-1.0
Program Spending	3.1	6.2	7.2

\* Consolidation of health & hospital board and school board operations and other entities plus accounting adjustments.

as a smaller Cabinet, fewer political staff and a wage freeze for the Legislature, political staff and senior bureaucrats for at least two years. A program is under way to assess all government expenditures, including the budgets of district health authorities, school boards, and other provincial agencies, as well as possible synergies with municipalities and Ottawa. Infrastructure investment will be scaled back from the FY10 peak. For the Province's employee pension plans, options to improve funding, beyond the contribution rate increases in recent years, will be considered.

**For Nova Scotia, achieving balanced books by FY11 appears to be a tall order**, even with slightly firmer natural gas prices recently and the Deep Panuke offshore project coming on stream in 2010. Scotia Economics' view that Nova Scotia's real GDP will decline in 2009, not edge higher as assumed in the *Budget*, with prices also weaker this year, results in a significantly lower nominal GDP estimate for 2010, even with our outlook for a stronger rebound. Looking ahead, the government's objectives such as working towards more efficient service delivery will benefit the Province, while minding the risks that remain as an economic recovery takes hold.

### Major Budget Highlights

#### Revenues

**Personal Income Tax (PIT)** cuts, through a four-year \$1,000 rise in the basic personal amount and a similar 13.83% increase in other nonrefundable credits, will be completed, with the last two stages in January 2009 and 2010. The new Transit Tax Credit scheduled for 2009 and the extension of the Healthy Living Tax Credit for adults will both be deferred, but a tax credit for up to \$500 annually in children's sports fees can be claimed as of 2009.

**The Graduate Retention Rebate** will replace the Graduate Tax Credit as of January 2009, offering for six years a \$2,500 annual tax credit for university graduates staying in Nova Scotia, and a \$1,250 annual tax credit for college graduates.

**The Tobacco Tax**, as outlined by the prior administration, rose by 5¢ per cigarette effective June 23, 2009 (\$21 million revenue boost for FY10).

**The Equity Tax Credit**, extended for two years to December 2011, will be enhanced from 30% to 35% of a resident's investment in a Nova Scotia small business, co-operative or community redevelopment initiative as of January 1, 2010, with the maximum annual credit lifted from \$15,000 to \$17,500.

**For the Harmonized Sales Tax (HST)**, the **New Home Construction Rebate** will rebate half of the 8% provincial portion of the HST, up to \$7,000 on the purchase or building of 1,500 new homes that began construction on or after January 2009 and will be largely completed by March 2010 (\$10½ million FY10 cost). "**Your Energy Rebate**" will be expanded to include a rebate of the 8% provincial portion of the **Harmonized Sales Tax (HST)** on residential electricity usage below the current 27.4 kWh threshold as of October 1 (\$15 million FY10 cost).

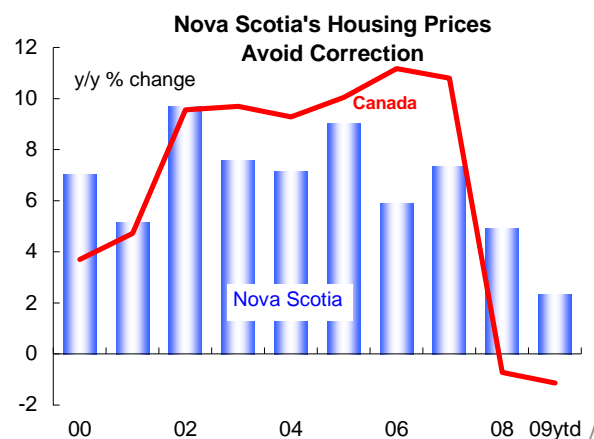
**The Large Corporations Tax** on the capital of non-financial institutions declined from 0.2% to 0.15% in July 2009, and previously scheduled annual declines will continue until the tax is eliminated in 2012.

**An Investment Credit for manufacturers and processors** of 10% will be introduced in January 2010 (\$25 million annual cost).

#### Expenditures

**For health care**, a provincial advisor is now in place to lead emergency care improvement. A \$750,000 fund will be established to cover travel and accommodation policy for families with a member requiring out-of-province treatment. For long-term care homes, security deposits will be eliminated.

**In K-12 education**, the Province will continue to run the Nova Scotia School Accreditation Program, reviewing each school's performance



### **Major Budget Highlights** (continued)

and student achievement. Increased co-operative education opportunities will be expanded, as will the Options and Opportunities program focused on community-based learning.

**Post-secondary** tuition fees will be frozen for all students through the 2010-11 academic year. For the **Nova Scotia Crown Share University Infrastructure Trust Fund**, the government is still working with post-secondary institutions to maximize its benefits.

**The Industrial Expansion Fund**, which recently helped to secure the contract to build nine patrol vessels in Nova Scotia, in the future will include in each project decision an independent analysis, currently being developed.

**Infrastructure** for FY10 of \$796 million includes \$325 million for highway construction and maintenance, \$140 million higher than FY09. When operating expenditures for roads and highways are added to the capital plan, the designated revenues from the Motive Fuel Tax and vehicle registrations falls \$107 million short of the estimated \$430 million total. Capital grants in FY10 will total \$88 million to District Health Authorities, \$32 million for social housing and \$2 million for specific requests from entities such as InNOVAcorp and the Trade Centre Limited. As province-wide broadband access is completed by year-end, workshops will be offered to communities receiving the service.

**For the Sydney Tar Ponds and Cove Ovens clean-up**, a \$400 million project to be completed by 2014, contracts continue to be awarded, including a \$52 million agreement for solidifying and stabilizing sediment in the tar ponds. The experience gained from the extensive clean-up is expected to enhance the province's expertise in remediation work.

**Municipalities** will receive \$2.8 million annually, phased in over three years, as a grant-in-lieu of tax payments for court houses owned by the Province.

**In the forest products sector**, a company's investment in its existing newsprint mill to make book-grade paper will be supplemented by \$2.5 million through the Community Development Trust Fund established by Ottawa in 2008. Book-grade paper is expected to witness more stable demand and prices in the targetted UK, EU and Asian markets.

### **Environmental Initiatives**

**The *Environmental Goals and Sustainable Prosperity Act*** will continue to guide environmental policy.

**Regulated caps on greenhouse gas (GHG) and air pollutant emissions for power generation facilities** have been introduced for 2010, 2015 and 2020 following a discussion paper and consultations earlier this year. The Province's goal is to cut total provincial GHG emissions by at least 10% from 1990 levels by 2020. The major power utility operating in Nova Scotia is responsible for roughly half of the province's GHG emissions and is therefore critical to the Province's climate change objectives. The Province plans to consult with interest groups on policy and regulatory approaches to curtail other GHG emissions sources. The Province's air quality regulations will be expanded to include caps on sulphur dioxide and nitrogen oxide emissions.

**For renewable electricity**, new targets announced in July call for 25% of Nova Scotia's power to be supplied from renewable sources by 2015. Release of a comprehensive renewable energy plan is planned for 2010 and consultations are under way to develop strategies to maximize the social, environmental and economic benefits of expanding renewable power generation.

**The Fundy tidal power demonstration project** has received approval, subject to strict conditions to protect the environment.

**Conservation policy** will include a goal of protecting at least 12% of Nova Scotia's land mass by 2015. Funds totalling \$81 million are currently set aside for parks, land purchases and land improvements. Integral to the Province's land protection efforts is the Wetland Conservation Policy, whose objectives include improving the stewardship of wetlands and preventing the net loss of wetlands by the end of 2009.

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