

Forecast Update



September 15, 2014

The Honourable Diana C. Whalen, Minister of Finance and Treasury Board

Overview

The Province of Nova Scotia is forecasting a deficit of \$274.5 million for 2014–2015, a decrease of \$4.5 million from the Budget Estimate of \$279.0 million. The variance is the result of increased Revenue, lower Departmental Expenses, lower Pension Valuation Adjustment, lower Debt Servicing Costs, and reduced Consolidation and Accounting Adjustments.

Total Revenues, including Net Income from Government Business Enterprises, are forecast to be \$9.6 billion, an increase of \$6.8 million. Total Expenses are forecast to be \$9.9 billion; \$31.0 million lower than budget. Changes in Consolidation and Accounting Adjustments result in a \$33.4 million negative impact to the bottom line.

Fiscal Summary 2014–2015

(\$ thousands)

GENERAL REVENUE FUND	Budget	Forecast	Increase (Decrease) from Budget
Revenue			
Ordinary Revenue	8,703,762	8,711,962	8,200
Ordinary Recoveries	521,983	521,153	(830)
Net Income from Government Business Enterprises	340,391	339,820	(571)
Total — Revenue	<u>9,566,136</u>	<u>9,572,935</u>	<u>6,799</u>
Expenses			
Departmental Expenses	8,851,640	8,829,553	(22,087)
Refundable Tax Credits	115,566	115,566	---
Pension Valuation Adjustment	90,505	84,235	(6,270)
Debt Servicing Costs	877,983	875,310	(2,673)
Total — Expenses	<u>9,935,694</u>	<u>9,904,664</u>	<u>(31,030)</u>
Consolidation and Accounting Adjustments for Governmental Units	90,602	57,232	(33,370)
Provincial Surplus (Deficit)	<u>(278,956)</u>	<u>(274,497)</u>	<u>4,459</u>

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Forecast Update

Ordinary Revenue Fiscal 2014–2015

(\$ thousands)

	Budget	Forecast	Increase (Decrease) from Budget
Provincial Revenue Sources			
Tax Revenue:			
Personal Income Tax	2,342,580	2,349,242	6,662
Corporate Income Tax	441,387	445,674	4,287
Harmonized Sales Tax	1,710,776	1,702,588	(8,188)
Motive Fuel Taxes	247,617	246,245	(1,372)
Tobacco Tax	226,722	224,885	(1,837)
Other Tax Revenue	154,993	155,025	32
Other Provincial Revenue:			
Registry of Motor Vehicles	121,458	121,458	---
Royalties—Petroleum	31,775	36,871	5,096
Other Provincial Sources	138,184	138,383	199
TCA Cost Shared Revenue—Provincial Sources	3,320	7,120	3,800
Other Fees and Charges	62,894	62,816	(78)
Prior Years' Adjustments	---	---	---
Investment Income:			
Interest Revenues	69,305	69,075	(230)
Sinking Fund Earnings	106,197	105,711	(486)
Total — Provincial Revenue Sources	<u>5,657,208</u>	<u>5,665,093</u>	<u>7,885</u>
Federal Revenue Sources			
Equalization Payments	1,757,744	1,757,744	---
Canada Health Transfer	846,774	846,774	---
Canada Social Transfer	331,895	331,895	---
Offshore Accord Offset Payments	64,481	64,481	---
Crown Share	13,762	14,788	1,026
Other Federal Sources	7,917	5,107	(2,810)
TCA Cost Shared Revenue	23,981	26,080	2,099
Prior Years' Adjustments	---	---	---
Total — Federal Revenue Sources	<u>3,046,554</u>	<u>3,046,869</u>	<u>315</u>
Total Ordinary Revenue	<u>8,703,762</u>	<u>8,711,962</u>	<u>8,200</u>
Net Income from Government Business Enterprises			
Nova Scotia Liquor Corporation	223,503	223,503	---
Nova Scotia Provincial Lotteries and Casinos Corporation	103,100	103,100	---
Halifax-Dartmouth Bridge Commission	12,143	11,572	(571)
Highway 104 Western Alignment Corporation	1,645	1,645	---
Total — Net Income from Government Business Enterprises	<u>340,391</u>	<u>339,820</u>	<u>(571)</u>

Revenues

Total Revenues, including Ordinary Recoveries of \$521.2 million and Net Income from Government Business Enterprises of \$339.8 million, are forecast to be \$9.6 billion, \$6.8 million more than the 2014–2015 Budget Estimates. This represents an increase in Ordinary Revenues of \$8.2 million, offset by a decrease in Ordinary Recoveries of \$0.8 million, and a decrease in Net Income from Government Business Enterprises of \$0.6 million.

Personal Income Taxes are up by \$6.7 million or 0.3 per cent from the 2014–2015 Budget Estimates as a result of slight increases in the projected levels of personal taxable income in both 2014 and 2015.

Corporate Income Taxes (CIT) are up by \$4.3 million or 1.0 per cent from the 2014–2015 Budget Estimates. This is due to increases in the levels of national corporate taxable income based upon federal estimates. The province's projected share of taxable income has also risen for both 2014 and 2015.

Harmonized Sales Tax (HST) is forecast to decline by \$8.2 million or 0.5 per cent from the 2014–2015 Budget Estimates as a result of a downward revision to the projected level of the residential housing investment tax base in 2014.

Motive Fuel Taxes are forecast to be down \$1.4 million or 0.6 per cent from the 2014–2015 Budget Estimates based upon lower projected consumption of both gasoline and diesel oil, primarily as the result of higher projected prices for both gasoline and diesel oil.

Tobacco Tax revenues are forecast to decline by \$1.8 million or 0.8 per cent from the 2014–2015 Budget Estimates as a result of the consumption of cigarettes being lower than projected and the Consumer Price Index for tobacco products growing faster than previously estimated.

Petroleum Royalties are forecasted to increase by \$5.1 million or 16.0 per cent from the 2014–2015 Budget Estimates based on higher estimates of production on the Deep Panuke project than previously projected.

Other Provincial Sources are forecast to be up by \$0.2 million or 0.1 per cent, primarily from improved results at the Resource Recovery Fund Board.

Other Fees and Charges are forecast to be down \$0.1 million or 0.1 per cent to \$62.8 million. The largest difference comes at Community Services where sub-lease revenue from Housing Nova Scotia decreased as the result of an office relocation to new premises.

Total investment income is forecast to be \$0.7 million or 0.4 per cent lower than budget. Interest Revenue is down \$0.2 million and Sinking Fund Earnings are down by \$0.5 million, primarily as a result of lower interest rates.

Crown Share Adjustment Payments are up by \$1.0 million or 7.5 per cent from the 2014–2015 Budget Estimates as a result of increased production and profitability associated with the Deep Panuke project.

Other Federal Sources are forecast to be down by \$2.8 million or 35.5 per cent primarily from a \$2.6 million reduction in Infoway funding as a result of changes to the project. There is also a \$0.2 million reduction in Building Canada funding because of project timing.

Ordinary Recoveries are forecast to be \$0.8 million or 0.2 per cent lower than Budget. This is primarily because recoveries at Education and Early Childhood Development are projected to be \$1.0 million lower than budget as a result of the finalization of a federal cost sharing agreement. Other changes include a \$0.4 million decrease at Community Services because of adjustments to previous year actuals for the maintenance of children; a decrease of \$0.2 million at Municipal Affairs due to lower Search and Rescue administration recoveries; an increase at Health and Wellness of \$0.2 million because of secondment and 811 service recoveries; \$0.2 million more than budget at Justice primarily because of increased salary recoveries at the Waterville facility from the IWK; and an increase of \$0.2 million at Communications Nova Scotia for salary and benefits as well as advertising services from external agencies.

The Halifax–Dartmouth Bridge Commission is forecasting to be \$0.6 million or 4.7 per cent below budget for net income primarily because of lower than expected traffic volumes.

Forecast Update

Expenses

Total expenses for 2014–2015 are forecast to be \$9.9 billion, \$31.0 million lower than budget. A decrease in Departmental Expenses account for \$22.1 million of the variance, while the

Pension Valuation Adjustment is \$6.3 million lower and Debt Servicing costs are \$2.7 million lower.

Departmental Expenses Fiscal 2014–2015

(\$ thousands)

	Budget	Forecast	Increase (Decrease) from Budget
Agriculture	60,968	61,488	520
Communities, Culture and Heritage	61,256	60,529	(727)
Community Services	903,496	902,762	(734)
Economic and Rural Development and Tourism	141,607	143,398	1,791
Education and Early Childhood Development	1,220,027	1,218,904	(1,123)
Energy	32,085	31,924	(161)
Environment	26,484	26,084	(400)
Finance and Treasury Board	13,529	13,418	(111)
Fisheries and Aquaculture	9,622	9,417	(205)
Health and Wellness	4,104,920	4,087,373	(17,547)
Internal Services	115,022	119,106	4,084
Justice	322,476	322,226	(250)
Labour and Advanced Education	348,420	347,878	(542)
Assistance to Universities	372,941	372,548	(393)
Municipal Affairs	157,792	156,355	(1,437)
Natural Resources	89,242	88,471	(771)
Public Service	240,151	237,997	(2,154)
Seniors	1,862	1,820	(42)
Transportation and Infrastructure Renewal	402,489	400,604	(1,885)
Restructuring Costs	227,251	227,251	---
Total Departmental Expenses	8,851,640	8,829,553	(22,087)

Note: Departmental variance is primarily related to mid-year forecast adjustments of \$29.4 million, offset by a net increase in expenses related to program spending of \$7.3 million.

Departmental Expenses

Total departmental expenses for 2014–2015 are forecast to be \$8.8 billion, or \$22.1 million lower than budget, primarily due to mid-year forecast adjustments offset by forecasted departmental pressures.

In mid-August departments were given direction by Finance and Treasury Board to make two mid-year forecast adjustments—a 1% reduction in departmental spending and a hiring slowdown. The 1% reduction has resulted in lower projected spending of approximately \$20 million and does not target major third-party grants, such as DHAs, school boards, salaries, or other support payments. The hiring slowdown requires departments to implement a 1:2 hiring ratio, meaning that one of every two vacant positions may be filled, resulting in estimated projected savings of \$10 million. These projected savings are partially offset by the following significant departmental variances:

The Department of Agriculture is forecasting to be \$0.5 million over budget due to an increase in Agri-Stability expenditures, related to the mink industry, of \$1.0 million, partially offset by the noted mid-year adjustments.

Economic and Rural Development and Tourism is forecasting to be \$1.8 million over budget of which \$2.1 million is due to Nova Star investment funding, as well as Capital Investment Incentives of \$0.8 million and an investment in the Innovacorp Demonstration Centre of \$0.6 million. These increases are partially offset by the noted mid-year adjustments.

The Department of Health and Wellness is forecasting to be \$17.5 million under budget primarily due to reduced capital grants because of project construction delays, as well as the noted mid-year adjustments.

The Department of Internal Services is forecasting to be \$4.1 million over budget due to capital and operating grants to Harbourside Commercial Park Inc. to purchase assets and land from ReNova Scotia Bioenergy, a provincially owned Crown corporation, and a grant to Nova Scotia Lands Inc. for operating expenses and capital grants related to the creation of a new commercial park located in Liverpool. The grants are partially offset by the noted mid-year adjustments.

The Department of Municipal Affairs is forecasting to be \$1.4 million under budget due to delays in several projects primarily related to the Building Canada Fund Communities Component funding totaling \$1.1 million, a reduction in planned expenses for the federally funded Search & Rescue New Initiatives program and the noted mid-year adjustments.

Public Service

The Public Service Offices are forecasting to be \$2.2 million under budget due to the noted mid-year adjustments, offset by Nova Scotia Business Inc. increases in forecasted payroll rebates of \$0.9 million.

Pension Valuation Adjustment

The Pension Valuation Adjustment has been updated to reflect changes to the Teacher's Pension Plan and market values from fund assets which has resulted in a \$6.3 million reduction in that expense.

Gross Debt Servicing Costs

Total Debt Servicing Costs are forecast to be \$2.7 million less than Budget because pension debt service costs have declined as a result of updated market values for pension fund assets.

Consolidation and Accounting Adjustments

Consolidation and accounting adjustments for government units are forecasted to be \$33.4 million below budget primarily due to District Health Authorities forecast amortization expense changes and Health and Wellness capital grant forecast reductions, offset by capital grants to Harbourside Commercial Park Inc. and Nova Scotia Lands Inc.

Capital Spending

Tangible Capital Assets (TCA)

The province is forecasting Capital Purchase Requirements to be on budget estimate with increased spending on buildings, vehicles, equipment, and land purchases offset by reduced IT project spending and reallocation of contingency funding.

Forecast Update

Capital Spending Forecast Fiscal 2014–2015

(\$ thousands)

	Budget	Forecast	Increase (Decrease) from Budget
Tangible Capital Assets:			
Highways and Structures	221,500	221,290	(210)
Buildings	131,276	134,339	3,063
Information Technology	45,347	41,755	(3,592)
Land Purchases	13,300	14,914	1,614
Vehicles and Equipment	23,065	25,184	2,119
Contingency	20,207	17,213	(2,994)
Total Departmental	454,695	454,695	0
Capital Grants	80,305	80,027	(278)
Total Capital Spending	535,000	534,722	(278)

Economic Performance and Outlook: 2014 and 2015

The 2014–2015 Budget Economic Assumptions were prepared with data and information up to March 4, 2014. Subsequently, new data and insights about the global and Nova Scotia economy have emerged. A revised economic forecast was published in the 2013–2014 Public Accounts in July (forecast date of June 17, 2014) and is reflected in the revenue forecast presented in this update. Some of the data released after the latest forecast date is discussed below and will be incorporated into future economic outlooks.

External Conditions

The global economy has kept broadly on track in recent months. The Canadian economy grew 3.1 per cent in the second quarter. Continued growth of around 2.5 per cent is expected, with a recovering Ontario economy and easing of growth in Alberta and Saskatchewan. The US economy rebounded in the second quarter, growing by 4.2 per cent. Further growth at an annualized rate of 3.0 per cent is anticipated over the near term. Euro Area economic growth remains weak while deflationary pressures mount, prompting further easing by the European Central Bank. The UK economy has seen robust GDP growth with healthier

inflation and falling unemployment. Japanese GDP has fluctuated around monetary stimulus and a value-added tax increase.

China is expected to continue to post solid, if unspectacular, growth. Other emerging market economies are expected to continue with healthy growth after adjusting to tighter financial conditions.

Current Economic Outlook for Nova Scotia

For 2014, aggregate growth is little changed from the Budget assumption, but the underlying composition of growth is shifting from domestic to international sources. Export performance has exceeded expectations while residential construction and labour markets have fallen short of the Budget assumption. Real GDP is forecasted to grow 1.4 per cent in 2014 before picking up to 1.9 per cent in 2015.

So far in 2014, Nova Scotia's economy has generated better export levels than expected in the Budget assumptions. Energy exports are up due to Deep Panuke natural gas production, but non-energy exports have also increased across most sectors.

Provincial Economic Outlook: 2014 and 2015

(Per cent change, except where noted)	Budget 2014/15 (March 2014)		Revised (June 2014)	
	2014	2015	2014	2015
Real GDP (chained 2007 dollars)	1.4%	2.1%	1.4%	1.9%
Nominal GDP	2.9%	4.3%	3.0%	4.0%
Compensation of Employees	2.4%	4.0%	2.5%	3.8%
Household Final Consumption	2.5%	3.3%	2.6%	3.3%
Retail Sales	1.9%	2.5%	2.2%	2.5%
Consumer Price Index	1.5%	2.0%	1.6%	2.0%
Investment in Residential Structures	1.0%	2.0%	-3.0%	2.4%
Net Operating Surplus: Corporations	3.8%	3.6%	4.9%	5.1%
Exports of Goods to Other Countries	5.6%	4.6%	7.7%	4.6%
Population at July 1 (thousands)	939.5	939.3	939.5	939.3
Employment (thousands)	455.8	457.6	451.5	455.0
Unemployment Rate (Annual Average)	8.6%	8.4%	9.0%	8.4%

While international activities have been supportive of growth, domestic conditions have underperformed. Employment and the labour force have both fallen in 2014. Over the January-August period employment decreased 1.7 per cent (-7,700) as the labour force dropped 1.8 per cent (-9,200). The employment decrease is concentrated in self-employment, while the declining labour force is primarily a phenomenon of an aging population. Although there have been smaller declines in payroll employment, wages have trended up, with average weekly earnings (including overtime) rising 3.6 per cent and total employee compensation increasing 2.1 per cent over the first half of the year.

Year-over-year CPI inflation was 2.0 per cent in July. Temporary inflation pressures can be attributed to higher energy prices and the effects of a depreciating Canadian dollar. Retail sales over the first six months are up 2.5 per cent with sales up at gasoline stations, general merchandise stores, and motor vehicle and parts dealers.

During the first half of the year, residential investment fell 19.6 per cent, primarily on falling investments in new dwellings. After a weak first quarter, building permits and housing starts have picked up, but elevated inventories, demographic pressures, flat prices, and new stricter mortgage requirements are expected to keep activity down in 2014. Non-residential building construction decreased by 5.9 per cent over the first half of the year.

Key Risks

There remain a number of risks to the forecast from external, national, and provincial sources that could result in changes to the outlook for 2014 and 2015.

Geopolitical conflicts in the Middle East and Ukraine have not yet caused dramatic movement in energy markets, but have the possibility for disruption with negative effects spilling over to the broader global economy. Central banks in several advanced economies (US, UK, Canada) are expected to raise target interest rates after several years of no movement creating potential for increased volatility in financial markets in 2015.

Nova Scotia's domestic economic conditions are sensitive to major project investments and other large events and initiatives. With more than half of the year complete, uncertainty around 2014 has diminished. Strong export performance could elevate the pace of growth for 2014, but the transmission of this positive risk into revenues is uncertain. There are offsetting negative risks in construction and labour markets. A number of key indicators are not yet known that could result in revisions including final Provincial Economic Accounts for 2013, imports, government spending, non-construction investment, and corporate profits. The specific risks around the Nova Scotia economy and forecast procedure noted in the Budget Assumptions remain.

*This document and other financial publications can be viewed
on the Department of Finance and Treasury Board website at:*

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