

December 19, 2008

Overview

The Province of Nova Scotia is forecasting a 2008-2009 budget surplus of \$212.9 million, an increase of \$23.3 million over the estimate at budget time.

Total revenues, including net income from Government Business Enterprises, are forecast to be \$8.5 billion, \$14.8 million more than budget. This is primarily due to the new federal crown share adjustment payment, offset by declines in income taxes and petroleum royalties.

Total expenses are forecast to be \$8.3 billion, \$15.9 million lower than budget. Increases in the pension valuation adjustment and expanded HARP and energy efficiency programs are more than offset by expenditure management and lower debt servicing costs.

The forecast allocates \$211.7 million of the \$212.9 million surplus to the debt.

Fiscal Summary Fiscal 2008–2009

(\$ thousands)

	Budget	Forecast	Increase (Decrease) from Budget
CONSOLIDATED FUND			
Revenue			
Ordinary Revenues	7,476,037	7,481,276	5,239
Fees and Other Charges	60,834	61,915	1,081
Ordinary Recoveries	456,375	468,492	12,117
Sinking Fund Earnings	114,400	108,100	(6,300)
Total Revenues	<u>8,107,646</u>	<u>8,119,783</u>	<u>12,137</u>
Expenses			
Departmental Expenses	7,360,889	7,349,333	(11,556)
Pension Valuation Adjustment	67,590	81,301	13,711
Debt Servicing Costs	904,522	886,435	(18,087)
Total Expenses	<u>8,333,001</u>	<u>8,317,069</u>	<u>(15,932)</u>
	<u>(225,355)</u>	<u>(197,286)</u>	<u>28,069</u>
Consolidation and Accounting			
Adjustments for Governmental Units	<u>56,800</u>	<u>49,294</u>	<u>(7,506)</u>
Net Income for Government Business Enterprises			
Nova Scotia Gaming Corporation	136,200	134,500	(1,700)
Nova Scotia Liquor Corporation	210,021	212,021	2,000
Other Enterprises	12,000	14,403	2,403
	<u>358,221</u>	<u>360,924</u>	<u>2,703</u>
Provincial Surplus	<u>189,666</u>	<u>212,932</u>	<u>23,266</u>
Allocation of Surplus			
Offshore Offset Agreement	105,884	105,884	---
Debt Retirement	71,437	105,816	34,379
Other	12,345	1,232	(11,113)
	<u>189,666</u>	<u>212,932</u>	<u>23,266</u>

Ordinary Revenue Fiscal 2008–2009

(\$ thousands)

	Budget	Forecast	Increase (Decrease) from Budget
Provincial Revenue Sources			
Personal Income Tax	1,828,653	1,784,420	(44,233)
Corporate Income Tax	415,902	386,541	(29,361)
Harmonized Sales Tax	1,151,027	1,156,389	5,362
Tobacco Tax	138,127	138,127	---
Motive Fuel Taxes	246,926	247,573	647
Interest Revenues	81,823	79,463	(2,360)
Registry of Motor Vehicles	98,122	100,874	2,752
Royalties—Petroleum	513,775	500,829	(12,946)
Other Provincial Revenues	284,338	288,502	4,164
Prior Years' Adjustments	---	(12,734)	(12,734)
TCA Cost Shared Revenue	2,692	2,792	100
Total—Provincial Revenue Sources	<u>4,761,385</u>	<u>4,672,776</u>	<u>(88,609)</u>
Federal Revenue Sources			
Equalization Payments	1,464,935	1,464,935	---
Offshore Oil and Gas Payments	105,884	105,884	---
Crown Share Adjustment Payment	---	95,100	95,100
Canada Health Transfer	664,185	668,683	4,498
Canada Social Transfer	296,869	297,114	245
Wait Times Reduction Fund	17,056	17,056	---
Other Federal Sources	40,029	43,856	3,827
C48 Trust Funds	38,767	35,767	(3,000)
C52 Trust Funds	24,547	22,234	(2,313)
Prior Years' Adjustments	---	7,299	7,299
TCA Cost Shared Revenue	62,380	50,572	(11,808)
Total—Federal Revenue Sources	<u>2,714,652</u>	<u>2,808,500</u>	<u>93,848</u>
Total—Revenue	<u>7,476,037</u>	<u>7,481,276</u>	<u>5,239</u>

Revenues

Total revenues, including net income from Government Business Enterprises of \$360.9 million, are forecast to be \$8.48 billion, \$14.8 million more than the 2008-2009 budget estimate. Consolidated Fund revenues are up by \$12.1 million.

Overall, provincial source revenues are down by \$88.6 million from the 2008-09 estimate.

Personal Income Taxes (PIT) are forecast to decline by \$44.2 million from the budget estimate due to a forecast decline in national personal taxable income. Nova Scotia's share and yield of the national taxable income from the budget estimate are below expectations and growth in national taxable income in 2009 has been revised downward.

Corporate Income Taxes (CIT) are forecast to decline from the budget estimate by \$29.4 million as federal forecasts of national corporate taxable income are revised downwards. Corporate profits in 2008 were strong but are anticipated to weaken significantly in light of the current global financial circumstances.

Harmonized Sales Tax (HST) is forecast to increase by \$5.4 million from budget, reflecting strong consumer spending in the year to date, which is likely to slow for the remainder of the year due to weakness in the Canadian economy.

Motive Fuel Taxes are forecast to be up slightly from the budget estimate by \$0.6 million as consumption increases with declining world oil prices. This has been partially offset by the recent weakening of the Canadian dollar relative to the US dollar which pushes gasoline and diesel prices slightly higher than they otherwise would have been.

Offshore royalties are forecast to decline by \$12.9 million from the 2008-2009 estimate, as earlier record high oil and gas prices have dropped significantly in recent months. This recent drop is slightly offset by the weakening Canadian dollar as the contracts are denominated in US dollars.

Other significant revenue variances include:

- an increase in Registry of Motor Vehicles revenues by \$2.8 million due to increases in both commercial and passenger vehicle registrations;
- a decrease in Interest revenues of \$2.4 million due to a decline in interest recovery;
- an increase in Other Provincial Source revenues of \$4.2 million.

Prior Year Adjustments from provincial sources are forecast to decline \$12.7 million, due to a number of changes to various provincial taxes and royalty revenues.

Overall, federal source revenues are up by \$93.8 million from the 2008-09 estimate.

Equalization and the Offshore Accord Payments are based upon the province's election to receive payments calculated according to the Expert Panel approach. This is a one-estimate, one-payment approach and as a result the forecast is equal to the budget estimate. The Province will not receive any guarantee payment in 2008-2009 pursuant to the clarification reached with the federal government in October 2007.

The Crown Share Adjustment Payment is forecast to be \$95.1 million. This figure was not available at the time the 2008-2009 budget was tabled and as a result was not included in the estimate.

The Canada Health Transfer (CHT) and the Canada Social Transfer (CST) are forecast to increase by \$4.7 million based on new federal estimates of the province's share of the national pool to be distributed.

Other federal source revenues are forecast to be \$3.8 million higher than budget. This is made up of a reduction in medical equipment funding of \$1.2 million and an increase of \$5.0 million in funding for geological research examining the potential for carbon storage in Nova Scotia. This funding was announced in the 2008 federal budget and is offset by a matching expenditure increase.

C48 and C52 Trust funds are forecast to be \$5.3 million lower as a result of reduced draw-downs from federal trusts established for Affordable Housing Infrastructure (\$3.0 million), and Patient Wait Times Guarantee (\$2.3 million). These trust funds are drawn down in accordance with expenditures in these areas and are therefore offset by reduced expenditures in the departments of Community Services and Health.

Tangible Capital Asset cost-shared revenue from the federal government is down by \$11.8 million from the 2008-09 estimate. The majority of this decline is due to delays in recoveries from the Build Canada Fund and ecoTrust.

Prior Year Adjustments from federal sources are forecast to be \$7.3 million as a result of new population estimates for the open years of the Canada Health Transfer and the Canada Social Transfer.

Ordinary Recoveries are forecast to be \$12.1 million higher than budget. This is primarily as a result of increased recoveries at Transportation and Infrastructure Renewal for highway maintenance and storm damage repairs, increased recoveries from the federal government for early learning and child care funding at Community Services and various increases at Service Nova Scotia and Municipal Relations and the Department of Justice.

Net Income for Government Business Enterprises

Net Income from Government Business Enterprises is forecast to be \$360.9 million, which is \$2.7 million higher than budgeted.

The Nova Scotia Liquor Corporation's net income is up \$2.0 million due to higher sales and reduced operating costs.

The Halifax-Dartmouth Bridge Commission is forecasting an increase of \$1.0 million due to the elimination of a reserve for tokens.

Highway 104 Western Alignment Corporation is forecasting an increase in net income of \$1.4 million due to an increase in toll subsidy revenue received from the province. An offsetting expense item is recorded in Transportation and Infrastructure Renewal.

These increases are offset by a \$1.7 million decline in net income forecast by the Nova Scotia Gaming Corporation. Lower than budgeted ticket and video lottery revenues are partially offset by higher than budgeted casino revenues.

Departmental Expenses Fiscal 2008–2009

(\$ thousands)

	Budget	Forecast	Increase (Decrease) from Budget
Agriculture	59,563	60,261	698
Community Services	912,570	908,525	(4,045)
Economic Development	91,645	97,950	6,305
Education and Universities	1,492,255	1,491,166	(1,089)
Energy	21,817	33,977	12,160
Environment	44,607	44,923	316
Finance	29,871	28,521	(1,350)
Fisheries and Aquaculture	7,463	7,463	---
Health	3,205,939	3,192,672	(13,267)
Health Promotion and Protection	87,526	86,326	(1,200)
Justice	262,244	260,915	(1,329)
Labour and Workforce Development	62,443	61,876	(567)
Natural Resources	84,638	86,511	1,873
Public Service	156,350	153,467	(2,883)
Seniors	2,127	1,867	(260)
Service Nova Scotia and Municipal Relations	254,539	276,683	22,144
Tourism, Culture and Heritage	56,727	61,449	4,722
Transportation and Infrastructure Renewal	350,875	333,091	(17,784)
Restructuring Costs	177,690	161,690	(16,000)
Total—Departmental Expenses	<u>7,360,889</u>	<u>7,349,333</u>	<u>(11,556)</u>

Expenses

Total expenses for 2008-2009 are forecast to be \$8.3 billion, \$15.9 million less than budget. Savings in program spending and debt servicing costs are partially offset by higher pension expenses and expanded HARP and energy efficiency programs.

Recent global financial and economic events have begun to affect the economies of Canada and Nova Scotia. As a result, growth in the key revenue sources of the province has begun to slow and this trend is expected to continue well into 2009.

Government initiated a review of its expenditure plans to see where it was possible to achieve savings. This was necessary to ensure that the province met its commitment to maintain a surplus and reduce debt.

All departments were asked to identify where they could achieve savings through administrative and operating efficiencies and to identify savings in programs where uptake was lower than expected. Departments also identified areas where implementation of new programs would not be proceeding as quickly as anticipated at budget time.

However, Departments were also asked to consider carefully the impact of these savings on client groups, business and industry. Some of these savings were redeployed within departments to offset other emerging pressures.

Departments identified total reductions of \$43.6 million in spending for the remainder of 2008-2009 (see *next page*). These offset potential increases and resulted in an \$11.6 million decrease in departmental spending. Departments will continue to monitor their spending with a view to living within their reduced allocations through the remainder of the year.

Transportation and Infrastructure Renewal is forecasting a reduction of \$17.8 million based on the determination that \$35.2 million of the Sysco Remediation Fund Provision would not be required, offset by \$17.4 million in additional spending pressures for roadwork, storm damage and increased amortization.

As part of the expense management initiative, the provision for Contract Negotiations, Workforce Adjustment and Government Restructuring was reviewed and the estimates refined which resulted in a \$16 million reduction in the Restructuring Costs appropriation.

The Department of Health has had lower than anticipated enrollments in the new Family Pharmacare program, decreased utilization of some programs, later requirements for staff hiring, and a few minor adjustments to program implementations. The department is forecasting overall savings of \$13.3 million.

The Department of Community Services forecasts a \$4 million saving from the current budget, due to lower than anticipated demand in the Pharmacare programs. The introduction of the Department of Health's Family Pharmacare program has contributed to these savings. As well, the caseload decline in Income Assistance payments freed-up money to cover a growing caseload and additional program spending in the Services for Persons with Disabilities sector.

The Department of Education has increased pressures for a preventative maintenance program and NSTU insurance premiums which have been more than offset by savings identified in Higher Education programs and vacant positions across the department resulting in a total forecasted underspend of \$1.1 million.

Justice will achieve savings of \$1.3 million as a result of their efforts in controlling vacancies, and administrative and operating costs. Finance is forecasting savings of \$1.4 million due to vacancy management and reduced operating and amortization costs.

Health Promotion and Protection is achieving savings of \$1.2 million by controlling vacancies and managing administrative and operating costs. Nova Scotia Business Inc. is forecasting an underspend of \$2.1 million in the Strategic Investment Funds as NSBI clients have adjusted their growth projections.

The savings achieved by these departments are offset by overexpenditures in Service Nova Scotia and Municipal Relations of \$22.1 million primarily related to the enhanced Heating Assistance Rebate Program and administrative costs for the Energuide Loan Program.

Energy is forecasting \$12.2 million over budget as a result of increased participation in the EnerGuide and Smart Lighting Choices Programs, the new Heat Smart Program and the new Carbon Capture and Storage Research Consortium Project. The carbon capture project is offset by revenue.

Economic Development is forecast to be \$6.3 million over budget. This is due to increased investments through the Industrial Expansion Fund and an increase for Community Development Initiatives, offset by departmental savings.

Tourism, Culture and Heritage is forecasting \$4.7 million in additional spending. This is due to additional Strategic Community Investments and grants for locally managed museums, offset by savings from staff vacancies and operational savings. The \$1.9 million increase in Natural Resources is for fire fighting expenses related to the fire in Porters Lake/Lake Echo and some smaller fires in Shelburne as well as \$0.5 million for programs in the Renewable Resources Branch which have offsetting recoveries.

2008-2009 Expense Management Initiative

(\$ thousands)

Departments	Savings Achieved
Community Services	4,045
Economic Development	1,650
Education and Assistance to Universities	2,510
Energy	3,453
Environment	339
Finance	1,350
Health	13,267
Health Promotion and Protection	1,200
Justice	3,500
Public Service	
- Communications Nova Scotia	180
- Emergency Management Office	156
- Office of Immigration	230
- Legislative Services	600
- Nova Scotia Business Inc.	2,134
Seniors	260
Service Nova Scotia and Municipal Relations	4,027
Tourism Culture and Heritage	750
Transportation and Infrastructure Renewal	3,927
	<u>43,578</u>

The table above indicates the savings achieved by the departments as part of the Expense Management Initiative. The savings achieved may differ from the variance in the Departmental Expense table because some of the savings were redirected to offset critical pressures in the departments.

Gross Debt Servicing Costs

Gross debt servicing costs are forecast to drop \$18.1 million to \$886.4 million, compared to \$904.5 million estimated at budget.

Savings in interest expenses of \$23.5 million are primarily the result of reduced borrowing and a favourable currency transaction.

These are offset by a \$5.4 million increase in interest on pension and other obligations, related to revised actuarial assumptions and a valuation correction for 2006.

Pension Valuation Adjustment

The Pension Valuation Adjustment is forecast to increase by \$13.7 million to \$81.3 million. This increase is primarily the result of reduction in EARSL (Estimated Average Remaining Service Life) of plan members from 13 to 12 years, as well as a valuation correction regarding the December 31, 2006 position of the Teachers' Pension Plan.

Capital Spending

Gross capital spending has increased to \$374.4, \$33.0 million higher than the budgeted amount of \$341.4 million. This is primarily due to increases of \$36.3 million for highways and bridges offset by minor decreases in other capital projects.

Allocation of Surplus

The surplus is forecast to be \$212.9 million, an increase of \$23.3 million from estimate.

This includes a \$105.9 million legislated surplus from the Offshore Offset agreement, and further debt retirement of \$105.8 million.

Debt retirement is up \$34.4 million from budget. This relates to the increased spending on TCA referenced above.

The balance of the surplus is \$1.2 million.

Economic Performance and Outlook—2008

Nova Scotia's economy is growing at a slower pace than anticipated in the budget forecast, as positive results early in the year are offset by a number of negative trends.

The real Gross Domestic Product growth rate for calendar 2008 is now forecast at 1.4 per cent compared to a projected rate of 1.7 per cent at budget time. Private sector forecasters have also reduced their estimates for 2008.

Nova Scotia labour market conditions improved slightly in the first 11 months of 2008. Employment increased 1.3 per cent — compared to the budget forecast of 0.9 — and labour supply increased 0.9 per cent.

At the same time, the number of unemployed workers declined 4.4 per cent and unemployment dropped to 7.7 per cent, compared to 8.1 per cent forecast in the budget.

Consumer spending was the key driver of Nova Scotia's economy in 2008. Retail sales were up 5.7 per cent for the first ten months of 2008, well above the 4.4 per cent estimated at budget time. This was in large part due to a 7.6 per cent increase in new car sales.

Spending on residential capital investments increased 3.3 per cent for the January to September period of 2008, 0.5 percentage points higher than the budget forecast. Most of the growth came from new home construction, with an increase of 5.6 per cent, while renovation expenditures were up 1.4 per cent.

Consumer spending was supported by a 4.9 per cent increase in labour income for January to September, compared to the same period in 2007. This is slightly less than the 5.4 per cent growth anticipated at budget time.

The impact of the global economic situation can be seen in the drop in export sales to the slower moving United States economy.

Exports of key commodities like lumber, gypsum, shellfish, and newsprint and all other products — excluding natural gas — were down overall by 4.0 per cent until the end of September.

The economic situation also appears to be having an impact on jobs in the service sector. For the first 11 months of 2008 employment in business services was down 1.5 per cent while employment in the finance, insurance and real estate services sector was down 3.5 per cent.

Inflation has been higher than expectations with a 3.5 per cent increase in the Consumer Price Index for the first nine months of 2008, compared to the budget forecast of 2.0 per cent.

The current economic climate is expected to result in dampening consumer and business confidence going into 2009. Reduced confidence, declining credit access and already weak demand for exports is expected to impede consumer and business spending. Given these factors it is expected that there may be further pressure on provincial revenue sources as we move into 2009.

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www.gov.ns.ca/finance