

December 22, 2010

Overview

The Province of Nova Scotia is forecasting a surplus of \$97.2 million for 2010-2011, a difference of \$319.3 million over the estimate at budget time. This is the result of higher than expected revenues and lower expenses. Although progress is being made, the immense fiscal challenge still exists. The province still anticipates a significant deficit for the 2011-12 fiscal year – predicted to be \$370 million – as indicated in the four-year plan released with the spring 2010 budget.

A number of unexpected and one-time factors impacted the forecast, including \$97.6 million in Prior Year Adjustments, strong revenues from Personal Income Tax, savings from the Pension Valuation Adjustment and lower debt servicing costs. All contributed to a better than expected financial position.

While spending is down, this update does not include typical annual expenditures for university funding or

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Fiscal Summary Fiscal 2010–2011

(\$ thousands)

	Budget	September Update	Current Forecast	Increase (Decrease) from Budget
GENERAL REVENUE FUND				
Revenue				
Ordinary Revenue	7,623,118	7,608,688	7,828,541	205,423
Fees and Other Charges	62,537	62,721	62,646	109
Ordinary Recoveries	616,284	612,113	602,887	(13,397)
Sinking Fund Earnings	89,092	91,726	94,456	5,364
Total Revenues	8,391,031	8,375,248	8,588,530	197,499
Expenses				
Departmental Expenses	8,021,916	8,012,490	7,982,847	(39,069)
Tax Credits and Rebates	54,800	54,800	54,800	---
Pension Valuation Adjustment	8,448	9,012	(23,340)	(31,788)
Debt Servicing Costs	959,197	932,905	908,507	(50,690)
Total Expenses	9,044,361	9,009,207	8,922,814	(121,547)
	(653,330)	(633,959)	(334,284)	319,046
Consolidation and Accounting				
Adjustments for Governmental Units	82,674	82,551	75,410	(7,264)
Net Income from Government Business Enterprises				
Nova Scotia Gaming Corporation	116,400	116,400	123,600	7,200
Nova Scotia Liquor Corporation	223,459	223,459	223,433	(26)
Other Government Business Enterprises	8,714	8,346	9,063	349
	348,573	348,205	356,096	7,523
Provincial Surplus (Deficit)	(222,083)	(203,203)	97,222	319,305

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funding for student bursaries. An expense will occur next year and every year thereafter as the province transitions back to annual budgeting for these expenses.

Total revenues, including net income from Government Business Enterprises are forecast to be \$8.9 billion, an

increase of \$205.0 million from budget. Total expenses, including departmental expenses, tax credits and rebates, pension valuation, debt servicing costs, and consolidation and accounting adjustments are forecast to be \$8.8 billion, \$114.3 million lower than budget.

Budget Impact With University Funding

The Universities received \$341.6 million on March 31, 2010, for the 2010-2011 fiscal year. Had the payment to universities been included in the Budget, the impact would be as follows:

Budget Impact With University Funding Fiscal 2010–2011			(\$ thousands)
	Budget	Forecast	Increase (Decrease) from Budget
Revenue	8,739,604	8,944,626	205,022
Expense	8,961,687	8,847,404	(114,283)
Provincial Surplus (Deficit)	<u>(222,083)</u>	<u>97,222</u>	<u>319,305</u>
Payment to Universities made March 31, 2010	(341,642)	(341,642)	
Alternate Provincial Surplus (Deficit)	<u>(563,725)</u>	<u>(244,420)</u>	

Ordinary Revenue Fiscal 2010–2011

(\$ thousands)

	Budget	September Update	Current Forecast	Increase (Decrease) from Budget
Provincial Revenue Sources				
Personal Income Tax	1,896,905	1,879,875	1,968,378	71,473
Corporate Income Tax	343,620	343,620	337,341	(6,279)
Harmonized Sales Tax	1,413,115	1,420,106	1,442,821	29,706
Tobacco Tax	193,847	200,467	209,588	15,741
Motive Fuel Taxes	248,594	250,677	252,725	4,131
Interest Revenues	93,461	90,908	91,365	(2,096)
Registry of Motor Vehicles	108,720	109,538	109,555	835
Royalties—Petroleum	173,640	161,389	170,170	(3,470)
Other Provincial Revenues	264,569	277,408	277,816	13,247
Prior Years' Adjustments	---	(3,446)	97,649	97,649
TCA Cost Shared Revenue	9,650	9,780	10,231	581
Total—Provincial Revenue Sources	<u>4,746,121</u>	<u>4,740,322</u>	<u>4,967,639</u>	<u>221,518</u>
Federal Revenue Sources				
Equalization Payments	1,360,722	1,360,722	1,360,722	---
Offshore Oil and Gas Payments	227,225	227,225	227,225	---
Crown Share	33,498	33,498	29,717	(3,781)
Canada Health Transfer	724,564	724,564	728,602	4,038
Canada Social Transfer	307,575	307,575	309,233	1,658
Wait Times Reduction Fund	6,879	6,879	6,916	37
Other Federal Sources	42,742	42,742	42,742	---
C52 Trust Funds	3,415	3,415	3,415	---
Budget 2008 Trust Funds	16,283	16,436	16,436	153
Knowledge Infrastructure Program	38,003	37,611	37,611	(392)
Prior Years' Adjustments	---	---	(1,710)	(1,710)
TCA Cost Shared Revenue	116,091	107,699	99,993	(16,098)
Total—Federal Revenue Sources	<u>2,876,997</u>	<u>2,868,366</u>	<u>2,860,902</u>	<u>(16,095)</u>
Total—Revenue	<u>7,623,118</u>	<u>7,608,688</u>	<u>7,828,541</u>	<u>205,423</u>

Revenues

Total revenues, including net income from Government Business Enterprises of \$356.1 million are forecast to be \$8.9 billion, \$205.0 million more than the 2010-2011 budget estimate. This represents an increase in general revenues of \$197.5 million, and Net Income from Government Business Enterprises increasing by \$7.5 million. Provincial source revenues are up \$221.5 million from the 2010-2011 budget.

Personal Income Taxes (PIT) are forecast to increase by \$71.5 million from the budget estimate due to stronger national personal taxable income levels which recovered after declines in 2009-2010. Additionally, the province has a higher share of taxable income (2.5 per cent) compared to the budget estimate of 2.4 per cent.

Harmonized Sales Taxes (HST) are projected to increase by \$29.7 million as a result of an increase in the provincial tax base, based upon federal estimates received in November 2010. In addition, growth in consumer expenditures – which account for more than 70 per cent of HST revenues – is forecast to be stronger in 2010 and 2011 than anticipated for the 2010-2011 Budget Estimate.

Corporate Income Taxes (CIT) are expected to be down by \$6.3 million. Coming out of the recession, Nova Scotia's share of the national pool of corporate taxable income is down and profits for Nova Scotia corporations are growing at a slower rate nationally as corporations in other jurisdictions recover from more significant effects of the recession.

Tobacco Tax revenues are up \$15.7 million from budget. Consumption of legal tobacco products was expected to decline, but has increased above the original budget.

Motive Fuel taxes are forecast to be up from the budget estimate by \$4.1 million due to stronger than anticipated consumption, particularly diesel oil.

Offshore Royalties are forecast to decline by \$3.5 million from estimate primarily as a result of natural gas prices being lower than projected at budget time. A stronger Canadian dollar relative to the US dollar and lower production forecasts in 2011 also contribute to the decrease. The decline is partially offset by reduced operating and capital costs forecasted for 2011, higher world oil prices, and improved projections for gas production in 2010.

Interest revenues have declined \$2.1 million from budget, mainly due to a decline in projected interest associated with Housing Development Corporation loans.

Registry of Motor Vehicles revenues are up \$0.8 million due primarily to increases in both commercial and passenger vehicle registrations.

There is a positive Prior Year Adjustment from provincial sources of \$97.6 million, due to new federal estimates for prior years' provincial income taxes, HST, and the timing of Royalty Revenues which are offset by reduced Corporate Income Taxes.

Overall federal source revenues are forecast to decline \$16.1 million from the 2010-2011 estimate, mainly as a result of decreased spending on cost shared capital projects this year. A decreased estimate for Crown Share Adjustment Payments and a negative prior year adjustment for federal source revenues are offset by increases in the Canada Health Transfer and the Canada Social Transfer.

Equalization and the Offshore Oil and Gas Payments are provided on a one-estimate, one-payment approach and as a result the forecast is unchanged from the budget estimate.

Ordinary recoveries are expected to be \$13.4 million lower than budget primarily due to a \$9.0 million reduction at the Department of Labour and Workforce Development for labour market agreements, and a \$8.3 million decrease at the Department of Community Services primarily as a result of reduced expenditures on Early Childhood programs and delayed building projects at Housing, which are partially offset by increases of \$3.2 million at Transportation and Infrastructure Renewal for road, bridge, and building projects, and various small changes in other departments.

Net Income from Government Business Enterprises

Total Net Income from Government Business Enterprises is forecast to be \$356.1 million, up \$7.5 million from budget primarily as a result of higher than expected lottery earnings at the Gaming Corporation, and higher than budgeted traffic through the Cobequid Pass.

Departmental Expenses Fiscal 2010–2011

(\$ thousands)

	Budget	September Update	Current Forecast	Increase (Decrease) from Budget
Agriculture	60,879	60,866	60,872	(7)
Community Services	971,562	971,562	963,191	(8,371)
Economic and Rural Development	107,978	107,978	102,978	(5,000)
Education and Universities	1,376,008	1,376,889	1,375,293	(715)
Energy	35,943	35,943	35,943	---
Environment	52,777	48,635	48,648	(4,130)
Finance	33,870	33,870	33,790	(80)
Fisheries and Aquaculture	13,231	13,228	13,224	(7)
Health	3,634,935	3,634,935	3,628,088	(6,847)
Health Promotion and Protection	88,383	88,383	88,383	---
Justice	289,487	289,365	288,736	(751)
Labour and Workforce Development	182,918	176,580	172,926	(9,992)
Natural Resources	95,441	95,441	93,007	(2,434)
Public Service	194,467	192,854	190,452	(4,015)
Seniors	1,902	1,902	1,902	---
Service Nova Scotia and Municipal Relations	312,304	311,824	311,575	(729)
Tourism, Culture and Heritage	61,065	61,065	61,065	---
Transportation and Infrastructure Renewal	397,343	399,747	401,352	4,009
Restructuring Costs	111,423	111,423	111,423	---
Total—Departmental Expenses	<u>8,021,916</u>	<u>8,012,490</u>	<u>7,982,847</u>	<u>(39,069)</u>

Expenses

Total Expenses for 2010-2011 are forecast to be \$8.8 billion, \$114.3 million under budget due to delayed and reduced departmental expenses, pension valuation adjustment, debt servicing costs and consolidation and accounting adjustments.

Departmental Expenses

Total Departmental Expenses for 2010-2011 are forecast to be \$8.0 billion, \$39.1 million under budget.

The Department of Community Services is forecasting to be under budget by \$8.4 million. This is attributable to \$6.8 million less spending in Early Learning and Childcare because partners in the sector have experienced delays in spending allocated funds on approved expansion projects, and \$1.8 million less spending as a result of delayed completion of the Millwood Housing Project. Both are offset by reduced recoveries.

Economic and Rural Development is under budget by \$5.0 million because the uptake on the Manufacturing and Processing Investment Credit was less than anticipated. The program has been reprofiled to encourage investment in technologically-advanced machinery and equipment, and workplace training programs. The new program will now be called the Productivity Investment Program.

The Department of Environment is under budget by \$4.1 million primarily due to reduced spending on EcoTrust projects, as a result of higher than expected actual spending in 2009-2010.

The Department of Health is under budget by \$6.8 million as a result of an \$8.5 million reduction in capital grants related to construction delays at the Inverness Hospital, Community Living Bungalows, and the Radiation Therapy Wait Times project. The department is also reporting various pressures that are offset by other program savings, as well as operating and vacancy savings.

The Department of Labour and Workforce Development is forecasting to be under spent by \$10.0 million primarily due to reductions in labour market agreement programs. As these expenses are recoverable from the federal government, there will be a corresponding decrease in recoveries.

The Department of Natural Resources is under budget \$2.4 million primarily due to a delay in the completion of the rail bridge demolition at Bear River, Sissiboo River and Moose River, which will defer spending to future years.

Transportation and Infrastructure Renewal is forecasting to be \$4.0 million over budget primarily as a result of increased recoverable road work of \$3.2 million, and estimated repairs related to the storm damage at Meat Cove (\$0.2 million) and the November flooding on the South Shore (\$0.6 million), both of which are not recoverable from the Federal Disaster Assistance Program.

Public Service

The Treasury Board Office is transferring \$2.2 million from the Innovation Fund to TCA, as a result of the approval of capital projects.

NSBI is forecasting savings of \$1.2 million due to a reduction in payroll rebate payments through the Strategic Investment Fund.

Gross Debt Servicing Costs

Gross Debt Servicing Costs are forecast to drop by \$50.7 million to \$908.5 million, compared to \$959.2 million at budget. The change is a result of favourable interest rate movement resulting in savings of \$23.8 million and revised pension debt servicing costs of \$27.0 million, due to a change in the actuarial valuation of plan amendments.

Pension Valuation Adjustment

The Pension Valuation Adjustment is forecast to decrease by \$31.8 million to negative \$23.3 million, as a result of changes in the actuarial valuation of plan amendments.

Capital Spending

The Province is forecasting capital spending to be \$668.8 million in fiscal year 2010-2011, a decrease of \$41.8 million from the estimate at budget time. School and community college projects (\$10.1 million), government building projects (\$13.9 million), vehicle and equipment (\$3.7 million), information technology projects (\$2.7 million) and capital grants (\$11.6 million) are forecast to be under spent this year.

Savings on these projects are partially offset by a slight increase in cost for the de-construction of Queen Elizabeth High School (\$0.2 million). These under expenditures have resulted in the deferral of costs to 2011-2012 and have been reflected in the Capital Plan released on December 9, 2010. The following chart shows the capital budget forecast variances by spending category.

Capital Spending Forecast 2010–2011

(\$ thousands)

Category	Budget	Forecast	Variance
Highways	310,000	310,000	---
Buildings	189,966	166,000	(23,966)
Information Technology	42,664	39,965	(2,699)
Land and Land Improvements	14,090	14,255	165
Vehicles and Equipment	23,174	19,494	(3,680)
Total—Departmental	579,894	549,714	(30,180)
Capital Grants	130,710	119,133	(11,577)
Total Capital Program	710,604	668,847	(41,757)

Economic Performance and Outlook – 2010 and 2011

The Department of Finance has changed its economic outlook based on Statistics Canada data revisions, current indicators for prices, investment and employment, as well as looming risks to trade and investment. There are few changes to 2010 GDP growth, as weaker trade results were offset by robust investment while slow employment growth was offset by strong income. The outlook for 2011 is somewhat more positive in anticipation of a recovery in employment.

Provincial performance and outlook

Nova Scotia did not escape the recession in 2009. Real GDP and employment contracted 0.1 per cent.

Nova Scotia enjoyed steady employment growth from February to July 2010, but recent employment data became volatile, and then declined in the autumn. Overall employment grew by 0.2 per cent from January-November 2010, compared with the same period in 2009.

Slow employment growth in 2010 was offset by higher retail spending, labour income and construction investment. Retail sales (January-October 2010) were 5.7 per cent above the same period last year. This confirms the recovery observed in year-to-date labour income (+4.2 per cent) and average weekly wages (+3.5 per cent). Non-residential (+12.9 per cent) and residential (+19.9 per cent)

construction activities have supported construction jobs and wages, but this sector is expected to slow in 2011.

External conditions

Nova Scotia's trade and investment are sensitive to global, US and Canadian economic conditions. Globally, the withdrawal of fiscal stimulus and the sovereign debt crises threaten to dampen medium term growth. Improving private demand in both industrialized and developing countries is essential for recovery, particularly in the US.

Although Canada's employment has stabilized around its pre-recession peak and unemployment rates have fallen by more than one percentage point, rapid growth early in 2010 has slowed. Real GDP grew by 1.0 per cent (annualized) in Q3 2010.

US conditions are vital for Nova Scotia's trade outlook. Year-to-date international goods exports (+3.1 per cent) have fallen short of Budget expectations, especially as natural gas prices fell with supply from shale gas. Despite recent uncertainty, US real GDP grew by 2.5 per cent (annualized) in Q3 2010. US employment has also started to show improvement. Recovery in the US depends on private sector spending responses after recent tax changes and the period of stimulus spending. High fiscal deficits may push up interest rates, damaging long run consumer confidence and investment.

Economic Performance 2010–2011

(\$ thousands)

	2010-2011 Budget Assumption	December Forecast Update	2010-2011 Budget Assumption	December Forecast Update
	2010	2010	2011	2011
Real GDP (\$2002, % change)	1.9	1.9	1.2	1.5
Nominal GDP (% change)	4.4	3.9	2.7	2.5
Employment (% change)	1.2	0.3	0.3	1.3
Unemployment (average, %)	8.6	9.3	9.0	8.7
Personal Income (% change)	2.1	2.2	1.7	3.2
CPI (% change)	1.6	2.1	1.8	1.4
Retail Sales (% change)	3.1	5.6	1.8	2.9
Corporation Profits (% change)	17.2	11.0	9.0	5.2
Exports (% change)	8.3	4.0	9.4	5.2

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www.gov.ns.ca/finance