

August 31, 2005

## Overview

The Province of Nova Scotia is projecting a slightly larger surplus than originally budgeted for 2005-2006, as higher revenues and savings in some areas offset additional investments in economic development and various unanticipated costs.

The surplus is expected to grow by \$6.5 million to \$69.8 million, of which \$57.1 million is a legislated surplus to be applied to the debt.

Total revenues are up \$8.1 million, largely due to higher provincial own-source revenues.

Net debt servicing costs are estimated to be \$12.4 million lower than budgeted. This is attributed to lower-than-expected costs of servicing the debt and early receipt of \$830.0 million from the Government of Canada under the Offshore Offset Agreement.

## Fiscal Summary Fiscal 2005–2006

(\$ thousands)

	Budget	Forecast	Increase (Decrease) from Budget
<b>CONSOLIDATED FUND Revenue</b>	<b>6,097,580</b>	<b>6,105,713</b>	<b>8,133</b>
<b>Expenses</b>			
Net Program Expenses	5,496,275	5,519,017	22,742
Pension Valuation Adjustment	24,379	24,379	–
Net Debt Servicing Costs	897,468	885,065	(12,403)
<b>Total Expenses</b>	<b>6,418,122</b>	<b>6,428,461</b>	<b>10,339</b>
	<b>(320,542)</b>	<b>(322,748)</b>	<b>2,206</b>
<b>Consolidation and Accounting Adjustments for Governmental Units</b>	<b>37,191</b>	<b>45,871</b>	<b>8,680</b>
<b>Net Income for Government Business Enterprises</b>			
Nova Scotia Gaming Corporation	160,900	160,900	–
Nova Scotia Liquor Corporation	177,070	177,070	–
Other Enterprises	8,664	8,664	–
	<b>346,634</b>	<b>346,634</b>	<b>–</b>
<b>Provincial Surplus</b>	<b>63,283</b>	<b>69,757</b>	<b>6,474</b>
<b>Components of the Debt Reduction Plan</b>			
Debt Retirement – Contingency	4,000	4,000	–
Offshore Offset Agreement	57,100	57,100	–
Other	2,183	8,657	6,474
	<b>63,283</b>	<b>69,757</b>	<b>6,474</b>

## Revenues

Total revenues are forecasted to be \$8.1 million more than budgeted for 2005-2006, primarily due to higher than anticipated provincial own-source revenues.

Nova Scotia's corporate income tax revenues are now estimated to be up by \$11.1 million, reflecting updated information from the federal government.

Offshore royalties have increased by \$8.0 million as a result of the continued strength of natural gas prices.

These increases are offset, in part, by an \$8.4 million decline in Harmonized Sales Tax; there was a small decrease in Finance Canada's 2005 estimate of the HST Declared Revenue Pool.

In addition, the Province is projecting motive fuel tax revenue to drop by \$2.6 million as higher prices affect consumption.

For this forecast, no changes are being made to federal transfers or personal income taxes. Data on these sources are typically available in the fall. Current national and provincial data as well as economic trends, however, continue to support budget estimates from these revenue sources.

## Revenue Fiscal 2005–2006

(\$ thousands)

	Budget	Forecast	Increase (Decrease) from Budget
<b>Provincial Revenue Sources</b>			
Personal Income Tax	1,553,568	1,553,568	–
Corporate Income Tax	350,177	361,292	11,115
Harmonized Sales Tax	1,068,935	1,060,519	(8,416)
Tobacco Tax	177,567	177,567	–
Motive Fuel Taxes	256,895	254,326	(2,569)
Interest Revenues	72,413	72,413	–
Registry of Motor Vehicles	87,716	87,716	–
Royalties - Petroleum	30,000	38,000	8,000
Other Provincial Revenues	239,333	239,336	3
<b>Total—Provincial Revenue Sources</b>	<b>3,836,604</b>	<b>3,844,737</b>	<b>8,133</b>
<b>Federal Revenue Sources</b>			
Equalization Payments	1,343,527	1,343,527	–
Offshore Oil and Gas Payments	57,100	57,100	–
Canada Health Transfer	596,611	596,611	–
Canada Social Transfer	257,408	257,408	–
Other Federal Sources	6,330	6,330	–
<b>Total—Federal Revenue Sources</b>	<b>2,260,976</b>	<b>2,260,976</b>	<b>–</b>
<b>Total—Revenues</b>	<b>6,097,580</b>	<b>6,105,713</b>	<b>8,133</b>

## Net Program Expenses

Program spending is forecasted to be \$22.7 million higher than budgeted to cover additional economic development investments, unanticipated costs in emergency measures and health, and expenses for provincial enumeration.

The budget forecast for the Office of Economic Development has been increased by \$14.3 million to cover investments in Ocean Nutrition, the purchase of the Lunenburg waterfront lands, and additional business incentives provided under the Industrial Expansion Fund.

An additional \$3.3 million is required by Legislative Services to cover the costs of the provincial enumeration.

The Department of Health's forecast has been adjusted upward by \$2.8 million to reflect faster recruitment of staff at the Amherst hospital and increased operating costs related to the new beds at the Valley hospital.

The Emergency Measures Organization's forecast has been increased by \$1.9 million to cover some of the costs of flooding caused by heavy rains in May 2005. This is the Province's share of funding for flood damage eligible for Government of Canada assistance. The disaster also added \$0.3 million in non-eligible costs to the forecast of the Department of Transportation and Public Works.

Net Program Expenses Fiscal 2005–2006			(\$ thousands)
	Budget	Forecast	Increase (Decrease) from Budget
Agriculture and Fisheries	44,113	44,091	(22)
Community Services	716,174	716,174	–
Education and Universities	1,281,088	1,281,383	295
Energy	9,619	9,619	–
Environment and Labour	27,947	27,938	(9)
Finance	16,858	16,858	–
Health	2,559,740	2,562,526	2,786
Justice	107,847	107,847	–
Natural Resources	63,098	63,096	(2)
Public Service	183,455	202,849	19,394
Service Nova Scotia and Municipal Relations	96,384	96,384	–
Tourism, Culture and Heritage	42,383	42,383	–
Transportation and Public Works	263,954	264,254	300
Restructuring Costs	83,615	83,615	–
<b>Total - Net Program Expenses</b>	<b><u>5,496,275</u></b>	<b><u>5,519,017</u></b>	<b><u>22,742</u></b>

## Net Debt Servicing Costs

Net Debt Servicing costs are projected to decrease by \$12.4 million to \$885.1 million compared to the budget estimate of \$897.5 million.

This is due to lower short-term interest rates and savings generated by the early receipt, in June 2005, of \$830 million from the Government of Canada for the Offshore Offset Accord.

By August 25, 2005, the full \$830 million had been used to retire short-term government debt, saving borrowing costs to reissue that debt. Both the Dominion Bond Rating Service and Moody's Investor Service changed their rating outlooks on provincial debt to "positive" in the last two months, citing as a contributing factor the Offshore Offset Agreement monies being paid directly to debt.

The Province of Nova Scotia continues to borrow in domestic capital markets to refinance maturing debt issues. To date, the Department of Finance has capitalized on the current low interest rate environment by issuing two long-term debt issues (for a total of \$350 million) at interest rates of under 5 per cent.

## Consolidation and Accounting Adjustments

The consolidation and accounting adjustments summarize the estimated impact on the provincial surplus of governmental units controlled by the Province. These adjustments eliminate transactions between the units in the government reporting entity.

Of the \$8.7 million variance in consolidation adjustments, \$8.5 million relate to the capital grant to the Waterfront Development Corporation for the purchase of the Lunenburg waterfront lands and the operating grant to Innovacorp in relation to the Ocean Nutrition initiative.

## Economic Performance and Outlook—2005

Nova Scotia's real Gross Domestic Product for 2005 is expected to be in line with the 2.1 per cent growth projected in the budget. This is consistent with the latest survey of private sector economists, who are forecasting a 2.2 per cent growth rate.

While employment growth is slightly slower than expected at budget time, the unemployment rate has been averaging very close to the budget forecast of 8.5 per cent for 2005. Labour income is performing well.

Retail sales growth remains positive and the housing construction market, compared to last year, has been stable.

The relatively high value of the Canadian dollar continues to affect the Nova Scotia economy. Investment in machinery and equipment is up, resulting in a boost to productivity. However, the exchange rate, combined with declining natural gas production, has put downward pressure on the level of export sales.

Manufacturing shipments remain positive, but the rate of growth has been declining. High commodity prices and low interest rates are helping to offset the high exchange rate.

Inflation, as measured by the Consumer Price Index, has been running above expectations, due to high energy prices and an increase in electric utility rates.