



**PROVINCE OF
NEWFOUNDLAND
AND LABRADOR**

**HIGHLIGHTS
AND
ANALYSIS**

**Consolidated Summary
Financial Statements**

**Public Accounts
31 March 2005**

TABLE OF CONTENTS

Purpose	1
Summary	1
The Public Accounts Volumes	1
Financial Summary - 31 March 2005	3
Consolidated Accrual Result Compared to Original Budget (Accrual)	3
Consolidated Accrual Result Compared to Previous Year	4
Highlights - Financial Position	5
Net Debt and Net Borrowings	6
<i>Net Debt per Capita</i>	6
<i>Net Borrowings per Capita</i>	7
Highlights - Financial Operations	8
Revenues	8
<i>Revenues by Source - 2005 and 2004</i>	8
<i>Total Revenues - 5 Year Comparison</i>	9
Expenses	11
<i>Expenses by Category - 2005 and 2004</i>	11
<i>Expenses by Sector - 5 Year Comparison</i>	12

Key Indicators	13
Flexibility	14
<i>Province's Interest Cost as a Percentage of Revenues</i> ..	14
<i>Provincial Revenues as a Percentage of GDP</i>	15
Sustainability	16
<i>Net Debt as a Percentage of GDP</i>	16
<i>Annual Deficit as a Percentage of GDP</i>	17
Vulnerability	18
<i>Foreign Currency Debt as a Percentage of Net Borrowings</i>	18
<i>Federal Transfers as a Percentage of Provincial Revenues</i>	19
Glossary of Terms	21

PURPOSE

These highlights are based on the audited Public Accounts for the year ended 31 March 2005. The purpose of this document is to provide users with accurate, relevant and understandable information on the financial position of the Province and the results of its operations.

SUMMARY

Government has improved the financial position of the province in the 2005 fiscal year. In spite of those improvements, government still faces significant financial challenges. The net debt of the province is still rising. The province's net debt at 31 March 2005 was \$11.9 billion, a significant amount. Each citizen's share of the provincial net debt for 2005 was \$22,982, the highest of all the provinces.

Government's challenge is to find a balance in meeting its social and other responsibilities to the people of the province while remaining vigilant in managing the province's financial situation.

THE PUBLIC ACCOUNTS VOLUMES

Volume I: Consolidated Summary Financial Statements

- These are the combined audited financial statements of the Consolidated Revenue Fund (all departments) and government organizations (including Health and School Boards) which are controlled by and therefore accountable to Government.
- They present the consolidated financial position of the Province on an accrual basis, in accordance with the accounting standards established for governments by the Canadian Institute of Chartered Accountants (CICA).

Volume II: Consolidated Revenue Fund (CRF) Financial Statements

- These are the audited financial statements of the Consolidated Revenue Fund (all departments) on an accrual basis.

Volume III: Consolidated Revenue Fund (CRF) Supplementary Statements and Schedules

- They present the revenues and expenditures, and the resulting annual surplus/deficit, of the Consolidated Revenue Fund on a cash basis.

Volume IV: Financial Statements of Crown Corporations, Boards and Authorities

- They comprise reproductions of the audited financial statements of each government organization (Crown corporations, boards and authorities).
- The Auditor General issued an unqualified audit opinion on the financial statements for 2004-05.
- The Public Accounts (excluding Volume IV) can be found on the Government's website at: www.gov.nl.ca/ComptrollerGeneral/Publications.htm
- Copies of all volumes of the Public Accounts can be obtained at the Queen's Printer, Confederation Building.

FINANCIAL SUMMARY - 31 MARCH 2005

- Volume I: Consolidated Summary (accrual) Deficit - \$488.8 million; Net Debt - \$11.9 billion; and Accumulated Deficit - \$9.8 billion.
- Volume II: CRF (accrual) Deficit - \$554.7 million; Net Debt - \$11.7 billion; and Accumulated Deficit - \$10.6 billion.
- Volume III: CRF (cash) Deficit - \$83.4 million; comprised of a Current Account cash surplus of \$143.6 million offset by a Capital Account cash deficit of \$227.0 million.

CONSOLIDATED ACCRUAL RESULT COMPARED TO ORIGINAL BUDGET (ACCRUAL)

The difference between the budgeted annual accrual deficit of \$839.6 million as per the 2004-05 Estimates and the actual accrual deficit of \$488.8 million is \$350.8 million. This difference occurred primarily due to the following:

- Total revenue was \$73.4 million more than originally budgeted. Some of the significant factors attributing to this difference in revenue included:
 - An increase in offshore royalties of \$143.3 million, which can be attributed to higher than expected world oil prices and increased production. In addition, royalty rates tied to price and production also increased proportionately.
 - A decrease in taxation revenue of \$67.4 million mainly due to decreases in provincial revenues relating to corporate income taxes and harmonized sales tax. Adjustments were the result of revised estimates applicable to previous years.

- Total expenses were \$277.4 million less than originally budgeted for in 2005. Some of the significant factors which account for this change include:
 - Debt expenses decreased by approximately \$137.5 million. \$83.0 million of this amount resulted from a reclassification, not reflected in original budget numbers, of debt expenses to grant expenses. This reclassification has been included in the numbers for 2004 and 2005, as well as subsequent budgets. \$19.0 million reflects the decrease in interest expense on the unfunded pension liability. The balance of the variance can be attributed to favourable interest rates and a stronger Canadian dollar, which impacted debt servicing costs for foreign debt.
 - Social sector expenses have decreased by \$170.2 million as compared to original budget.
 - Amortization of tangible capital assets was \$42.5 million higher than originally budgeted. The original budget reflected amortization of deferred revenues of \$28.9 million, however, this policy was changed and did not apply in the calculation of actual amortization expense for the year.
- Total borrowing requirements of \$308.5 million for the year were significantly less than the originally budgeted amount of \$766.1 million.

CONSOLIDATED ACCRUAL RESULT COMPARED TO PREVIOUS YEAR

The difference between the actual accrual deficit of \$488.8 million for 2005 and \$913.6 million for 2004 is \$424.8 million, a reduction of 46.5% over last year. This overall decrease is a combination of an increase in revenues and decrease in expenses.

- Total revenues increased by \$264.1 million over 2004. The most significant contribution to this change is the increase in offshore royalties, primarily due to increased oil prices and production.
- Total expenses decreased in all sectors, and by \$160.6 million overall. A general reduction of \$112.7 million in grants and subsidies is the major factor for this change.
- Total borrowing requirements of \$308.5 million for the year were \$398.0 million less than the requirements of \$706.5 million for 2004.

HIGHLIGHTS - FINANCIAL POSITION

- Net debt and accumulated deficit as at 31 March 2005 are comprised of the following components:

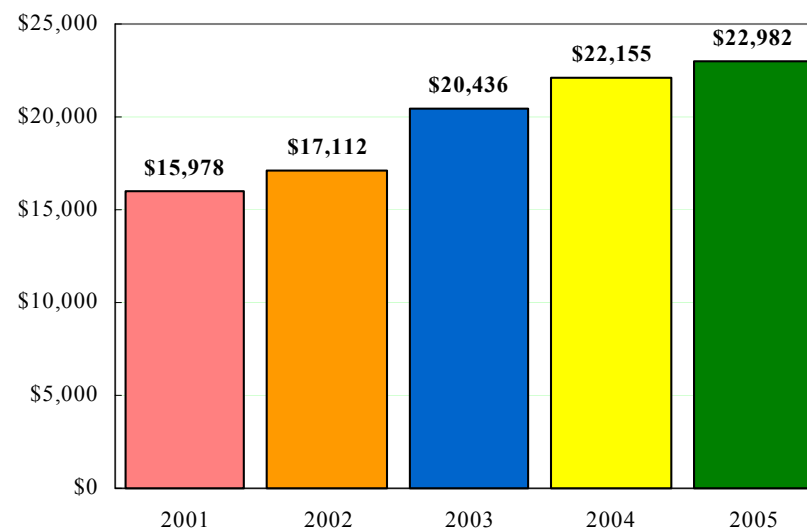
	<u>(\$ billion)</u>
Unfunded Pension Liability	3.93
Borrowings (net of sinking funds)	6.94
Group Health and Life Insurance Retirement Benefits	1.16
Other Liabilities	1.70
Less: Total Financial Assets	<u>(1.84)</u>
Net Debt	11.89
Less: Tangible Capital Assets	(2.08)
Less: Other Non-Financial Assets	<u>(0.06)</u>
Accumulated Deficit	<u><u>9.75</u></u>

Net Debt and Net Borrowings

For the fiscal year ended 31 March 2005, net debt totaled \$11.9 billion which included net borrowings of \$6.8 billion. As indicated below, these figures have increased on a per capita basis over the past five years.

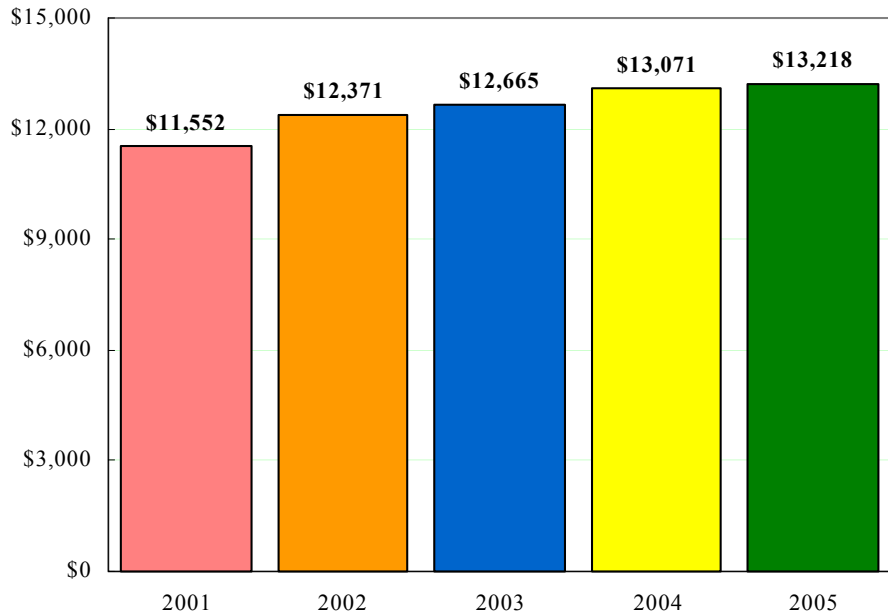
a) Net Debt per Capita

Net debt per capita indicates the average amount of provincial net debt owing by each citizen of the Province and is calculated by dividing the net debt of the Province by the Province's population. Each citizen's share of the provincial debt increased from \$22,155 in 2004 to \$22,982 in 2005, an increase of \$827 per person, as a result of an increase in the net debt combined with a slight decrease in the population.



b) Net Borrowings per Capita

Net borrowings per capita indicates the average amount of provincial debt owing by each citizen of the Province and is calculated by dividing the net debenture and other debt (net of sinking funds) of the Province by the population of the Province. Each citizen's share of the provincial debt increased from \$13,071 to \$13,218, a change of \$147 per person, between 2004 and 2005 primarily as a result of an increase in the debt combined with a slight decrease in the population. However, the increase is significantly less than the \$406 per person change between the two preceding years of 2003 and 2004.

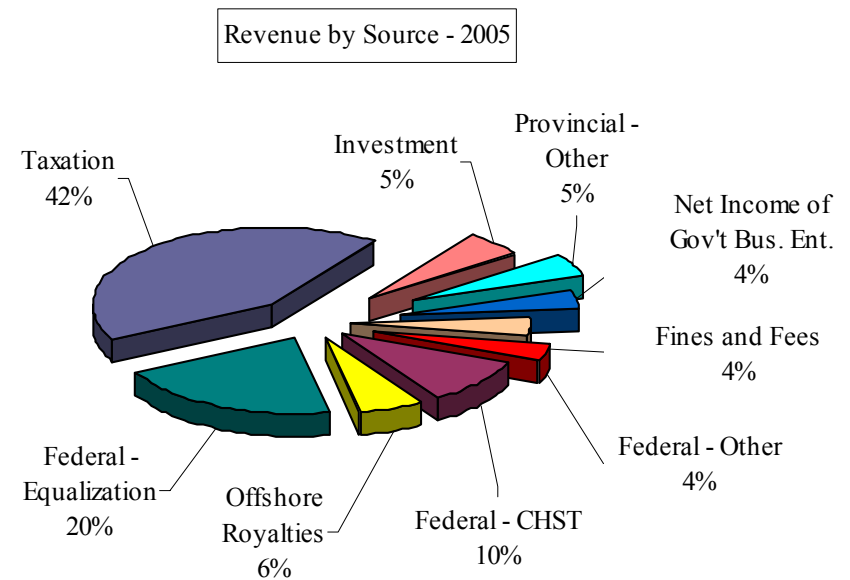


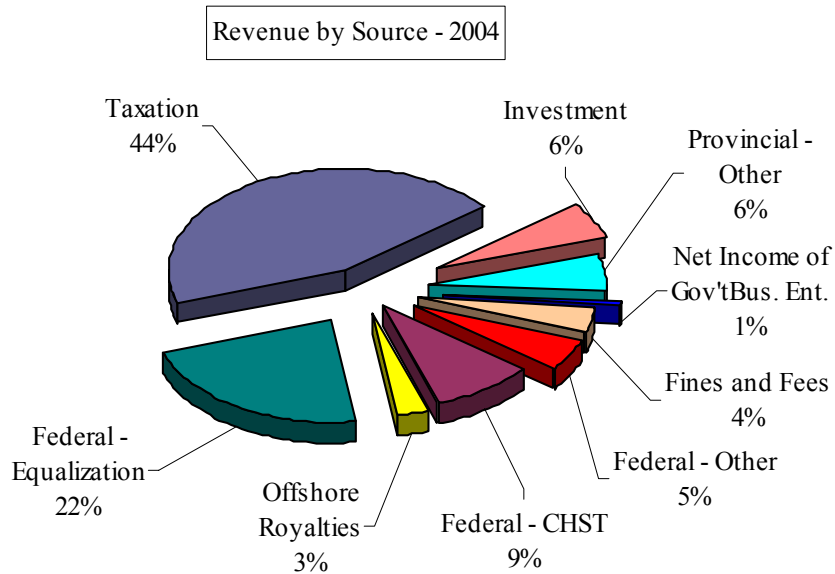
HIGHLIGHTS - FINANCIAL OPERATIONS

Revenues

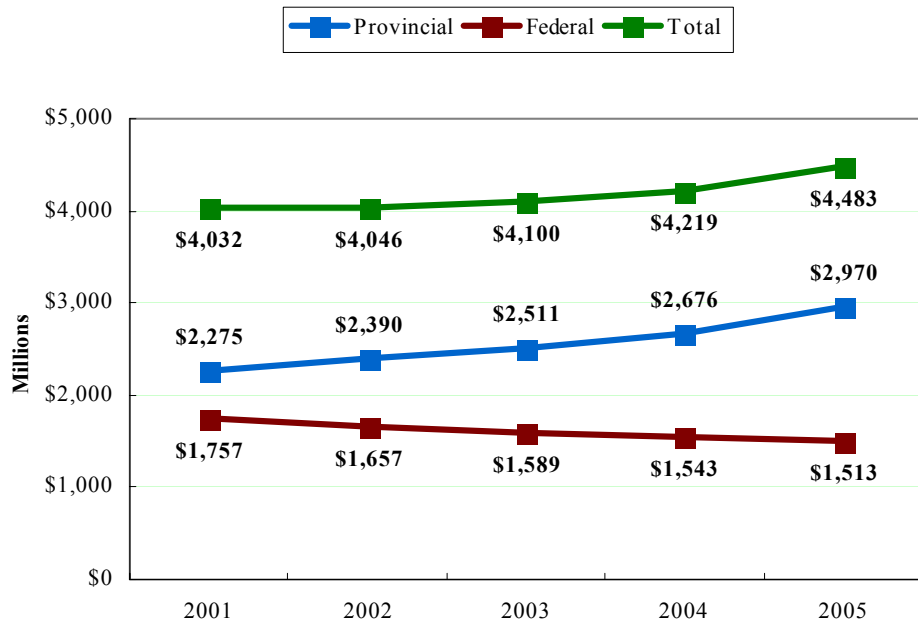
For the fiscal year ended 31 March 2005, total revenue amounted to \$4.5 billion. Of this amount, 33.8% came from Federal Government sources, while 66.2% was derived from provincial revenue sources. Details on these sources of revenue, including five-year historical comparisons, are provided in the following charts and graphs.

a) *Revenues by Source - 2005 and 2004*





b) Total Revenues - 5 Year Comparison



From an analysis of the above charts, the following observations can be made:

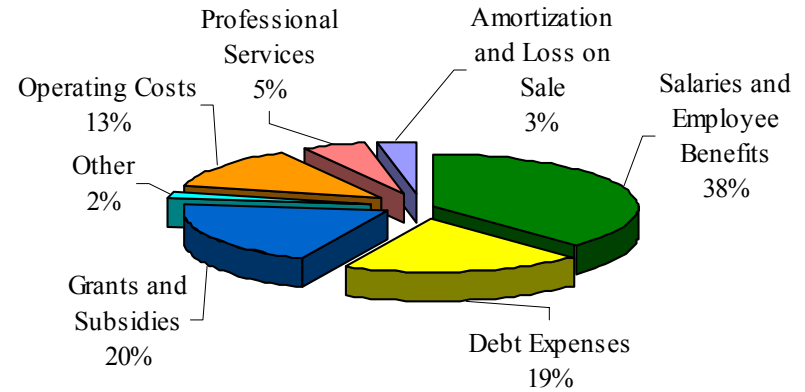
- Total revenues have been increasing over the last five years, ranging from \$4.03 billion in 2001 to \$4.48 billion in 2005, with an increase of \$264.1 million from 2004 to 2005.
- Total federal revenues have been steadily decreasing over the last five years, from \$1.76 billion in 2001 to \$1.51 billion in 2005; including a decrease of \$29.3 million from 2004 to 2005.
- Total provincial revenues have increased over the last five years, ranging from \$2.28 billion in 2001 to \$2.97 billion in 2005; including an increase of \$293.4 million between 2004 and 2005.
- Taxation remains the most significant source of revenues overall. However, taxation as a percentage of all revenues decreased slightly to 42.2% in 2005 from 44.0% in 2004.
- Offshore royalties increased between 2004 and 2005. This is primarily due to higher than usual oil prices and increased production.
- In 2004, the net income of Newfoundland and Labrador Hydro decreased due to a write-down of capital assets. Net income for 2005 has reverted to a rate comparable to previous years before the one time write-down.
- Equalization payments remain the most significant source of federal revenue representing 20.5% of all revenues (down slightly from 22.3% in 2004) and 60.8% of federal revenues in 2005.

Expenses

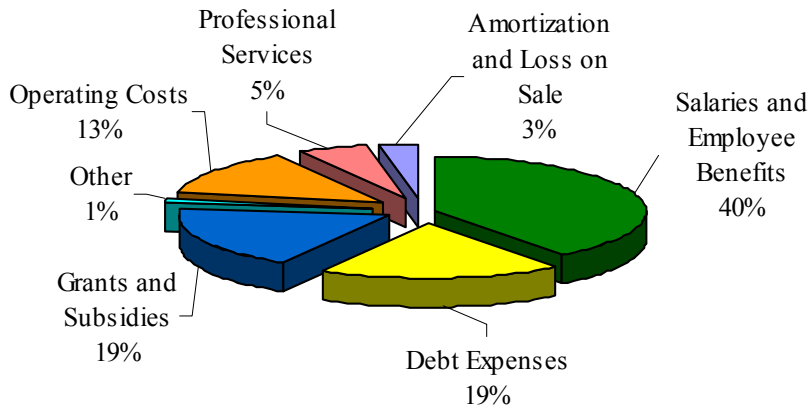
For 2005, total expenses amounted to \$5.0 billion. The following charts and discussion analyze the nature of these expenses by category and sector. In the discussion on expense by category, it should be noted that the 'Other' category represents capital property acquisitions, as well as amortization and loss on sale relating to tangible capital assets. As well, for the 5 year comparison of expenses by sector, the fiscal years 2003 to 2005 have been presented on the expense basis as a result of implementing a change in accounting policy relating to tangible capital assets. The 2001 and 2002 fiscal years are presented on the expenditure basis as the information necessary to make the appropriate adjustments was not readily available.

a) Expenses by Category - 2005 and 2004

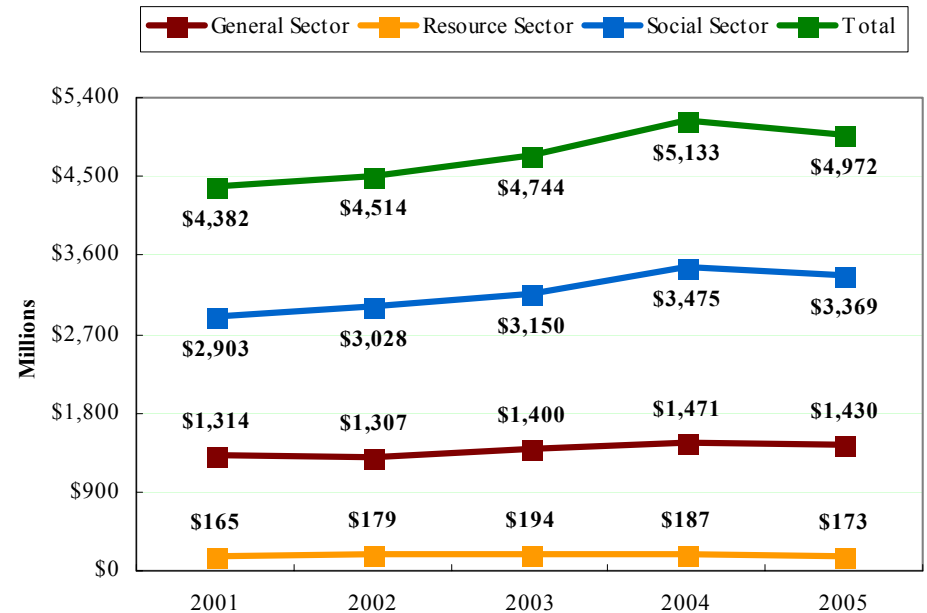
Expenses by Major Category - 2004



Expenses by Major Category - 2005



b) Expenses by Sector - 5 Year Comparison



From an analysis of the previous charts the following observations can be made:

- Total expenses increased by \$751.3 million from 2001 to 2004, then decreased by \$160.6 million to 2005, representing a change of 3.1% from 2004.
- Salaries and employee benefits remain the most significant expense.
- Together salaries/benefits and debt expenses represent 58.8% of total expenses for 2005, slightly higher than 57.0% in 2004.
- Expenses for the Social Sector which includes health, education and social services were \$3.4 billion in 2005, accounting for 67.8% of the total expenses for the year. Although the expense decreased overall from 2004 for the Social Sector by \$106.0 million, the percentage remains unchanged at 67.7% of total expenses.

KEY INDICATORS

- Key indicators included in this document provide a complete picture of the Province's financial condition at 31 March 2005.
- The common key indicators included herein were identified in a research report issued by the Canadian Institute of Chartered Accountants entitled *Indicators of Government Financial Condition*. These indicators, which are used in assessing a government's financial health in the context of the overall economic and financial environment, can be summarized under the headings of *sustainability*, *flexibility*, and *vulnerability*.

- While there are no established benchmarks for these indicators, one can assess the Province's financial condition through a comparison of previous years' indicators.
- Gross Domestic Product (GDP) and population figures were obtained from Newfoundland and Labrador Statistics Agency. Figures used were the latest non-forecasted information available as of 31 March 2005.

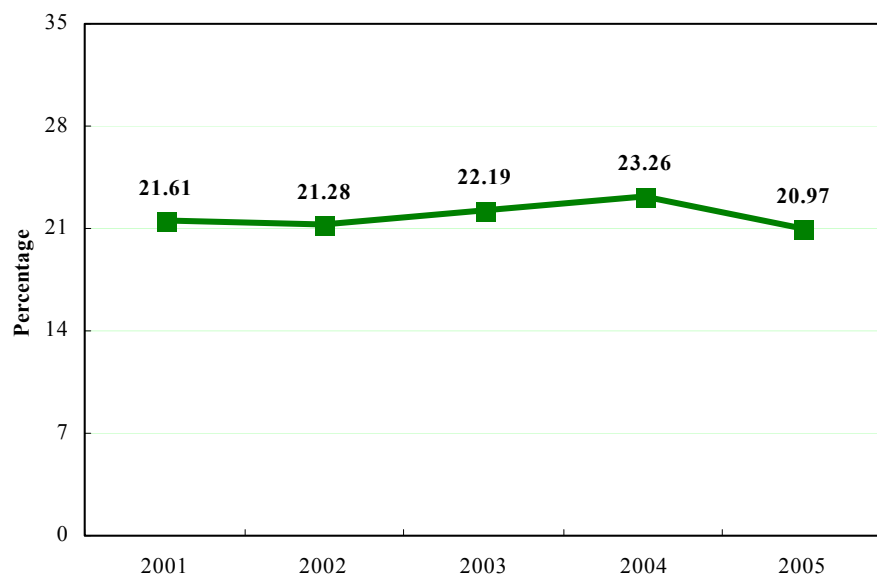
Flexibility

Flexibility refers to the degree to which a government can respond to rising commitments by either expanding its revenues or increasing its debt. Indicators of flexibility include:

a) Province's Interest Cost as a Percentage of Revenues

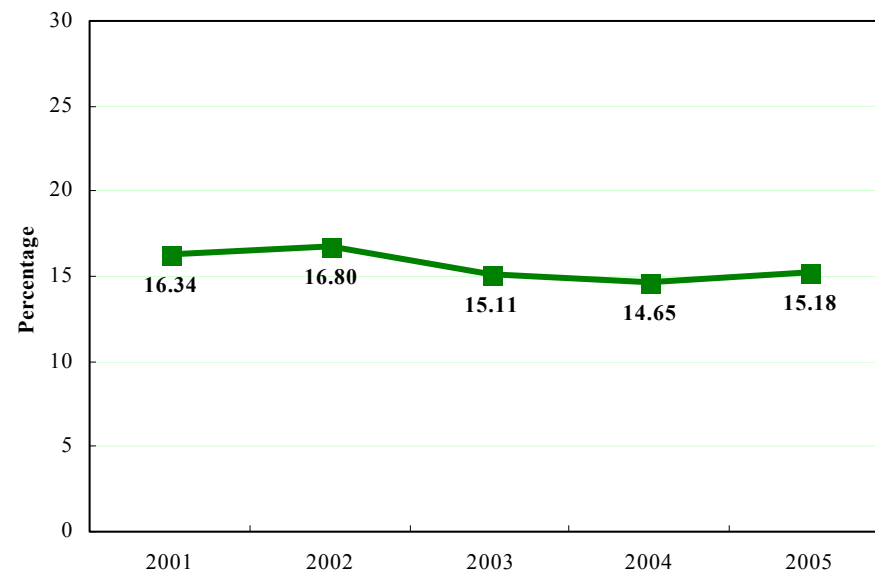
- This ratio measures the extent to which past borrowings may impact the Province's ability to provide for the economic and social needs of its citizens.
- The graph below indicates that the Province's interest cost as a percentage of revenues has stayed in the range of 20.97% to 23.26% over the past five years, peaking in 2004 with a decrease of 2.29% to its lowest level in 2005.
- The average of this ratio over the past five years is 21.86%. The relatively flat trend to this ratio indicates that interest costs remain a constant significant expense incurred by the Province since it represents 20.97% of all revenues.
- A reallocation of debt expenses to a correct categorization of grant expenses affected the graphs as presented in 2004 Highlights and Analysis

Booklet. For the purpose of this analysis, the expenses have been restated for the past five years.



b) Provincial Revenues as a Percentage of GDP

- The purpose of this indicator is to show the extent to which a government is taking income out of the economy in its jurisdiction, through both taxation and user charges.
- The following graph indicates that provincial revenues as a percentage of GDP have been fluctuating slightly over the last five years.
- The current year ratio is 15.18%, less than the five average of 15.62%. This suggests that on average, the Province is taking less income out of the economy (as a percentage) through taxation and user fees.



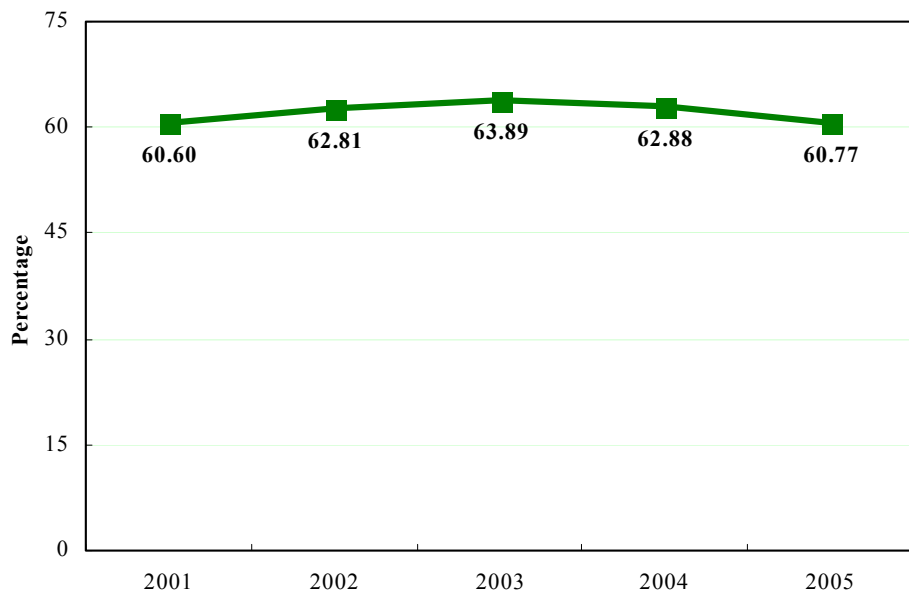
Sustainability

Sustainability refers to the degree to which a government can meet its existing program commitments and creditor requirements without increasing the debt burden on the economy. Indicators of sustainability include:

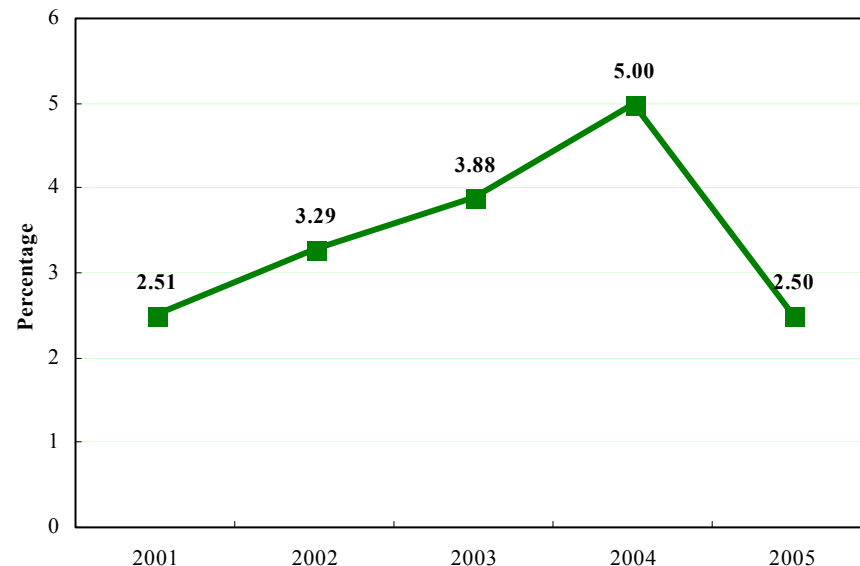
a) Net Debt as a Percentage of GDP

- This ratio measures the level of debt that the Province carries as a percentage of its GDP.
- As indicated in the following graph, net debt as a percentage of GDP has decreased over the last four years. This relationship implies that the rate of economic growth is greater than the rate of growth in debt. The lower this ratio, the more room Government has to manoeuvre in making fiscal choices.

- The average of this ratio over the past five years is 62.19%, with a slight decline from 62.88% in 2004 to 60.77% in 2005.



- The average of this ratio over the past five years is 3.44%.



b) Annual Deficit as a Percentage of GDP

- This ratio measures the difference between revenues and expenses expressed as a percentage of GDP.
- As indicated in the following graph, the annual deficit as a percentage of GDP increased from 2001 to 2004, despite a corresponding increase in GDP over the same period. However, the Province's annual deficits as a percentage of GDP decreased significantly in 2005 to a low of 2.5% in this five year period. If this decrease continues as a trend, the Province will increase its ability to meet financial obligations.

Vulnerability

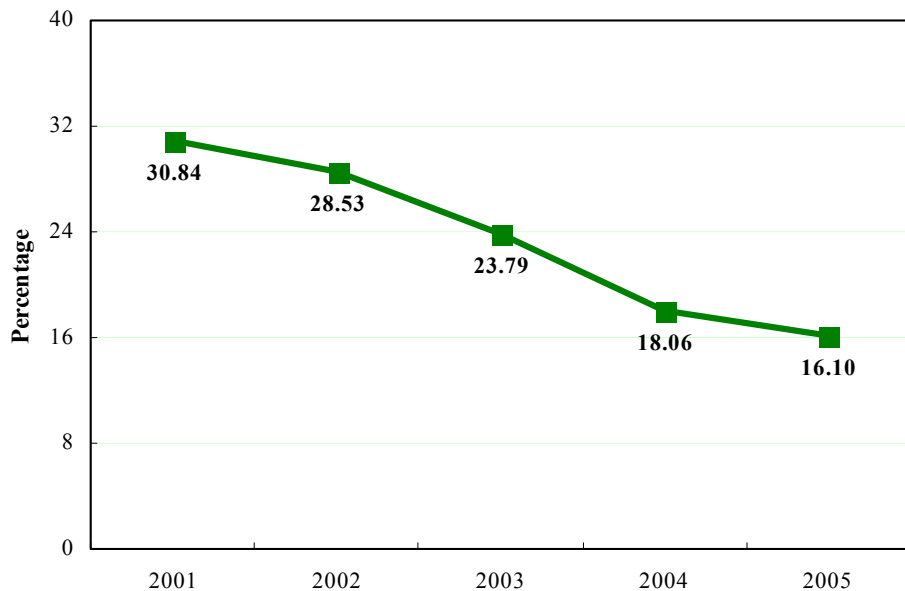
Vulnerability refers to the degree to which a government is dependent on, and therefore vulnerable to, sources of funding outside of its control or influence. Indicators of vulnerability include:

a) Foreign Currency Debt as a Percentage of Net Borrowings

- This ratio measures the amount of the Province's foreign currency debt relative to the Province's net borrowings. It reflects the degree of vulnerability to foreign currency swings that the Province faces.
- As indicated in the following graph, foreign currency debt as a percentage of net borrowings has decreased steadily over the last five years, thus

indicating that the Province is less susceptible to foreign currency fluctuations in terms of repaying its debt.

- The average of this ratio over the past five years is 23.46%, a decrease from the 2004 average of 26.94%. While this percentage indicates that foreign currency debt has historically represented a significant portion of the Province's borrowings, this ratio has now declined to a five year low of 16.10% for 2005.

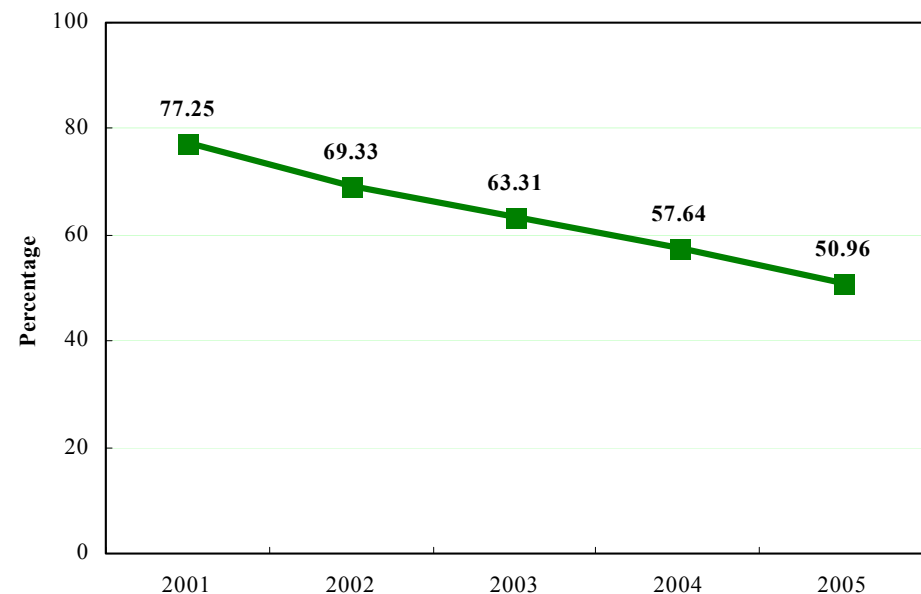


b) Federal Transfers as a Percentage of Provincial Revenues

- This ratio measures the extent to which the Province raises its own revenue from within the Province as compared to the extent it receives funds from the Federal Government.

- As indicated in the following graph, federal transfers as a percentage of provincial revenues have decreased over the last five years. This decline in federal transfers has placed a greater financial burden on the Province. Consequently, the fiscal policy decisions of the Federal Government have a significant impact on the Province's financial position.

- The average of this ratio over the past five years is 63.70%, down slightly from the 1999 - 2004 average of 67.73%. This percentage has decreased to 50.96% in 2005, indicating the Province's historically heavy dependence on the Federal Government is gradually being reduced.



GLOSSARY OF TERMS

<i>Accrual Basis:</i>	A method of accounting whereby revenues are recorded when earned/due and expenses are recorded when liabilities are incurred.
<i>Accumulated Deficit:</i>	Liabilities less total assets. This equals the net accumulation of all annual surpluses and deficits experienced by the Province.
<i>Annual Deficit:</i>	The excess of annual expenses over annual revenues.
<i>Cash Basis:</i>	A method of accounting whereby revenues are recorded when received and expenditures are recorded when paid.
<i>Financial Assets:</i>	Assets (such as cash, receivables and investments) to be used to reduce existing or future liabilities.
<i>GDP:</i>	Gross domestic product (at market prices) of the Province.
<i>Interest Cost:</i>	Interest on the Province's debt (e.g., borrowings, unfunded pension liability), as well as other debt related expenses.
<i>Net Borrowings:</i>	Total borrowings (debentures, treasury bills, etc.) less sinking funds. Also referred to as provincial debt in this report.
<i>Net Debt:</i>	Liabilities less financial assets.
<i>Non-Financial Assets:</i>	Assets consumed in the delivery of Government services, but not intended to reduce existing or future liabilities. Non-financial assets are primarily comprised of tangible capital assets.

Tangible Capital Assets: Non-financial assets which are held for use in the production or supply of goods and services and have useful economic lives extending beyond an accounting period. Examples include buildings, roads, infrastructure, marine vessels and heavy equipment and machinery.

Unfunded Pension Liability: The total unpaid pension benefits earned by existing/former employees and retirees less the value of assets set aside to fund the benefits.