Province of Newfoundland and Labrador

Public Accounts
Volume I

Consolidated Summary Financial Statements

For The Year Ended 31 March 2005

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INTRODUCTION

Volume I of the Public Accounts presents the consolidated summary financial statements of the Province of Newfoundland and Labrador. These statements are preceded by a report which discusses and analyzes the information contained within the summary financial statements. The report, entitled **Understanding the Financial Health of the Province of Newfoundland and Labrador**, provides a narrative review of the financial performance of the Province along with illustrations of key figures and relationships. This financial statement discussion and analysis, in conjunction with the consolidated summary financial statements, provides additional information for users of the Provinces' summary statements.

The consolidated summary financial statements combine the financial statements of the Consolidated Revenue Fund with the financial statements of various Crown Corporations, Boards and Authorities, as approved by Treasury Board, which are controlled by the Government of Newfoundland and Labrador. These organizations are accountable for the administration of their financial affairs and resources either to a Minister of the Government or directly to the Legislature.

These statements are prepared on the accrual basis of accounting in accordance with the Public Sector Accounting Board (PSAB) standards of the Canadian Institute of Chartered Accountants (CICA), and as outlined in the significant accounting policies of the Province. They are prepared by the Comptroller General of Finance and are audited by the Auditor General, who presents an annual report to the House of Assembly on the results of his audit. Budget figures, where available, are provided on several Statements for comparison purposes.

The Public Accounts for the year ended 31 March 2005 consists of three other volumes:

Volume II – Consolidated Revenue Fund Financial Statements presents the financial position of the Fund and the results of its activities.

Volume III – Consolidated Revenue Fund Supplementary Statements and Schedules presents the unaudited summary statements, detailed departmental statements, schedules and notes of the Fund and are prepared on a basis consistent with the Estimates of the Province.

Volume IV – Financial Statements of Crown Corporations, Boards and Authorities presents a reproduction of the available financial statements of the Crown Corporations, Boards and Authorities.

The Public Accounts of the Province are tabled in the House of Assembly in accordance with Section 60 of the *Financial Administration Act*.

<u>Internet Address</u>

The Public Accounts are available on the Internet at:
http:/www.gov.nl.ca/ComptrollerGeneral/publications.htm

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UNDERSTANDING THE FINANCIAL HEALTH OF THE PROVINCE OF NEWFOUNDLAND AND LABRADOR

Government is committed to the principles of transparency and accountability. In my role as the Minister of Finance and President of Treasury Board, I am reporting on the financial health of the province to the people of the province. A glossary of terms has been included in the pages that follow to assist the readers of this report and the Public Accounts.

Last year I noted in my report that government is committed to improving the financial position of the province so that future generations of Newfoundlanders and Labradorians will not have to deal with the consequences of fiscal mismanagement. I report that for the fiscal year ended 31 March 2005, the total borrowing requirements were $308 million as compared to $707 million for the 2004 fiscal year. The net debt of the province for the year ended 31 March 2005 increased by $447 million compared to $913 million for the 2004 fiscal year. The deficit for the year ended 31 March 2005 was $489 million compared to $914 million for the 2004 fiscal year. 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. As previously noted, the province had a significant deficit in 2005.

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.

LOYOLA SULLIVAN
MINISTER OF FINANCE AND
PRESIDENT OF TREASURY BOARD

23 September 2005

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THE PUBLIC ACCOUNTS VOLUMES

The Public Accounts consists of four volumes. These include:

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).
- The consolidated summary (accrual) deficit for the year ended 31 March 2005 as presented in Volume I is \$488.8 million; net debt is \$11.9 billion; and accumulated deficit is \$9.8 billion.

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.
- The CRF (accrual) deficit for the year ended 31 March 2005 as presented in Volume II is \$554.7 million; net debt is \$11.7 billion; and accumulated deficit is \$10.6 billion.

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.
- The CRF (cash) deficit of \$83.4 million for the year ended 31 March 2005 as presented in Volume III is comprised of a Current Account cash surplus of \$143.6 million offset by a Capital Account cash deficit of \$227.0 million.

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.
- In addition to the volumes of the Public Accounts, a **Highlights and Analysis** booklet is produced for the Consolidated Summary Financial Statements. This booklet may also be obtained from the above noted website or from the Queen's Printer.

The inclusion of this report, a financial discussion and analysis of the Public Accounts, is a practice recommended by the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants. The Public Sector Accounting Board sets the accounting standards for Canadian senior governments.

Information provided in this report will focus on the consolidated summary financial statements of the Province. Throughout this report, any reference to a particular year means the fiscal year ended in that year. For example, reference to 2005 means the fiscal year ended 31 March 2005.

GLOSSARY OF TERMS

To assist in understanding the discussion and analysis to follow in this report, definitions of the various terms used are provided below:

Accrual Basis: A method of accounting whereby revenues are recorded when earned/due and expenses are recorded when liabilities are incurred.

Accumulated Deficit: Liabilities less total assets. This equals the net accumulation of all annual surpluses and deficits experienced by the Province.

Annual Deficit: The excess of annual expenses over annual revenues.

Cash Basis: A method of accounting whereby revenues are recorded when received and expenditures are recorded when paid.

Financial Assets: Assets (such as cash, receivables and investments) to be used to reduce existing or future liabilities.

GDP: Gross Domestic Product (at market prices) of the Province.

Interest Cost: Interest on the Province's debt (e.g. borrowings, unfunded pension liability), as well as other debt related expenses.

Net Borrowings: Total borrowings (debentures, treasury bills, etc.) less sinking funds. Also referred to as provincial debt in this report.

Net Debt: Liabilities less financial assets.

Non-Financial Assets: 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.

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.

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.

- Additional variance analysis on the changes in revenues and expenses between the 2004 and 2005 fiscal years is included in later sections of this report.

CASH FLOW ANALYSIS

The Province records its transactions on an accrual basis in accordance with generally accepted accounting principles, the timing of which may vary from when actual cash is paid or received. In 2005, the Province's overall net cash inflows differed by $669.8 million from the previous year, as detailed in the following chart:

Cash flow by Category	**2005**	**2004**	**Difference**
	(000's)	*(000's)*	*(000's)*
Operating	116,583	(120,007)	236,590
Capital	(106,164)	(144,002)	37,838
Financing	424,891	264,521	160,370
Investing	46,930	(188,107)	235,037
Net Inflows (Outflows) of Cash	482,240	(187,595)	669,835

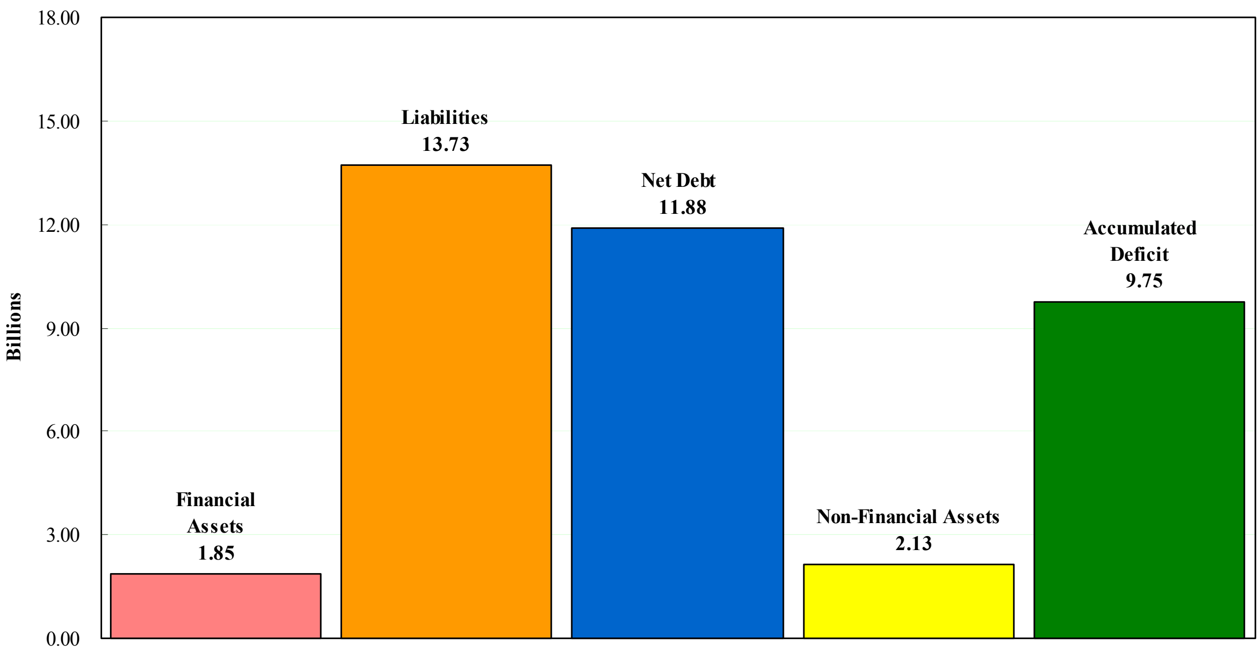
The main reason for the difference in the operating category is a positive cash impact related to a reduction in the annual deficit from 2004. A non-cash adjustment representing a write down in Newfoundland and Labrador Hydro assets of the previous year also impacted the cash flow from operations.

Cash inflows from financing increased by $160.4 million, mainly due to the $378.4 million received in the form of an interest-free equalization loan offset by an increase of $206.5 million in overall debt retirement.

Cash inflows from investing increased by $235.0 million during fiscal 2005, primarily as a result of a decrease in loan advances during the year by $167.7 million and a $59.4 million increase in loan repayments.

HIGHLIGHTS - FINANCIAL POSITION

The Province's annual deficit position improved in 2005 by $424.8 million, although net debt, borrowings and accumulated deficit continued to increase. The financial position as at 31 March 2005 is presented in the following chart.

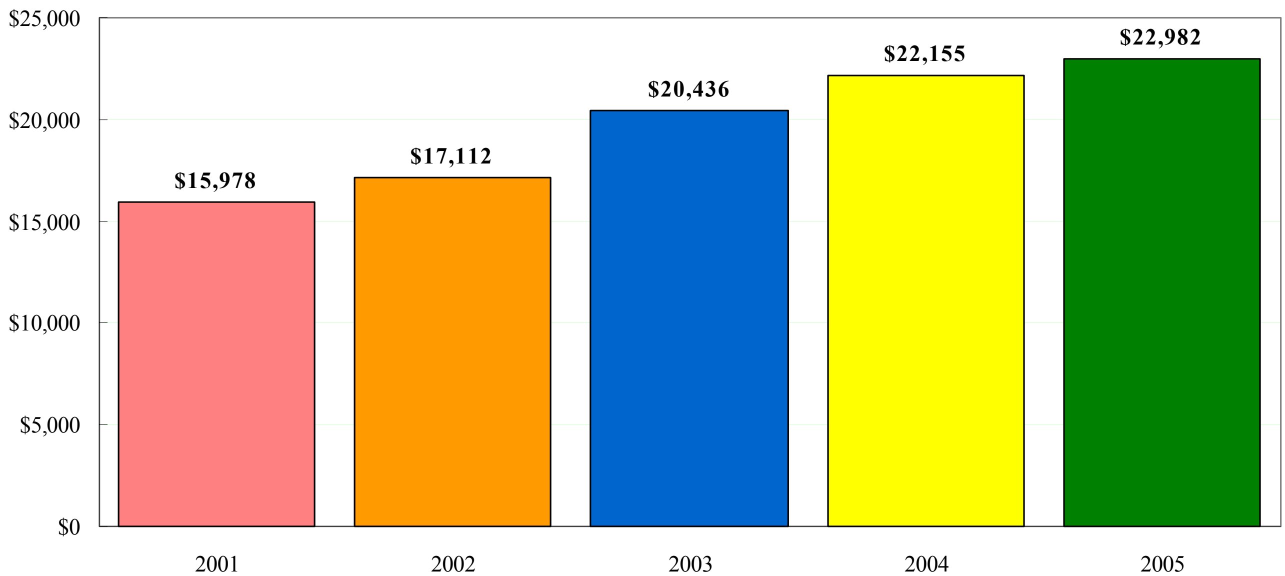


Net Debt and Net Borrowings

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.

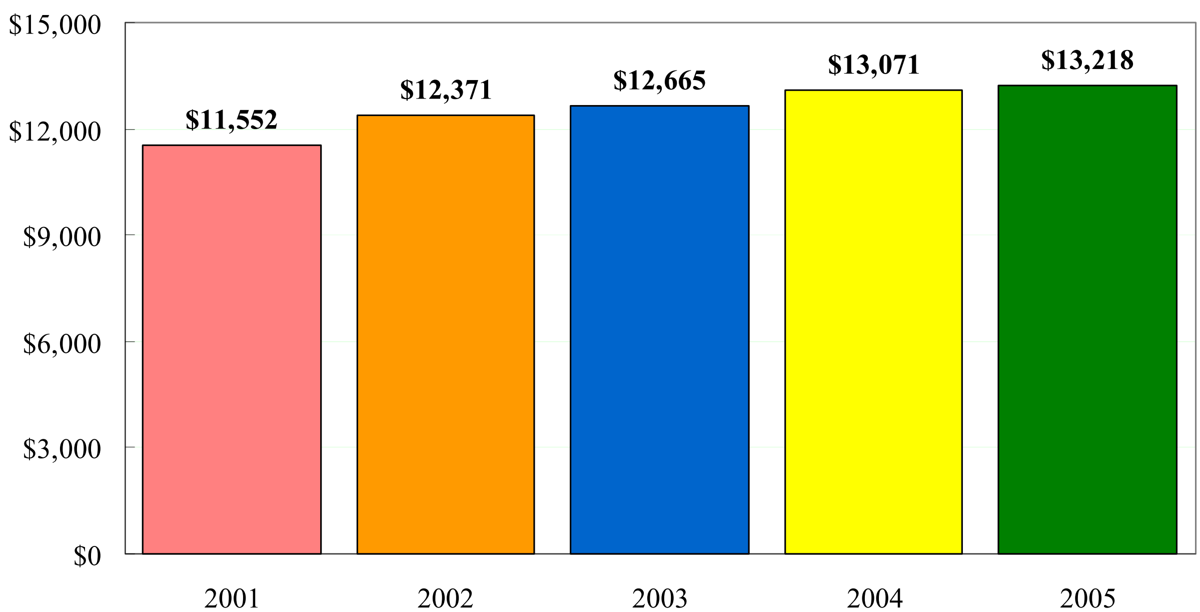
a) *Net Debt per Capita*

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.



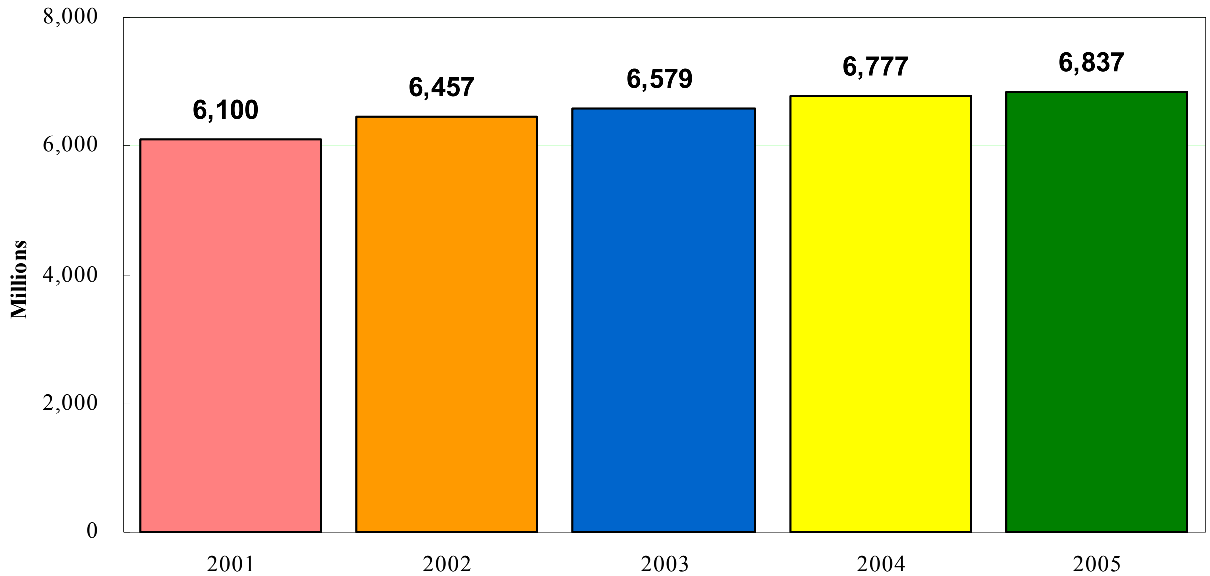
b) ***Net Borrowings per Capita***

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.



c) *Net Borrowings - 5 Year Comparison*

Net borrowings of the Province generally remained constant at $6.8 billion in both 2004 and 2005. Borrowings of the Consolidated Revenue Fund represented 89.2% of the total borrowings during 2005, a slight increase over 86.7% in 2004.



Non-Financial Assets

In 2005, non-financial assets of $2.1 billion related primarily to tangible capital assets. The net book value of tangible capital assets decreased by $44.1 million from 2004. Analysis of the following chart allows us to make these observations:

- Buildings and infrastructure (including roads, bridges, airstrips and marine facilities) represent 86.3% of the total net book value of tangible capital assets for the year ended 31 March 2005.

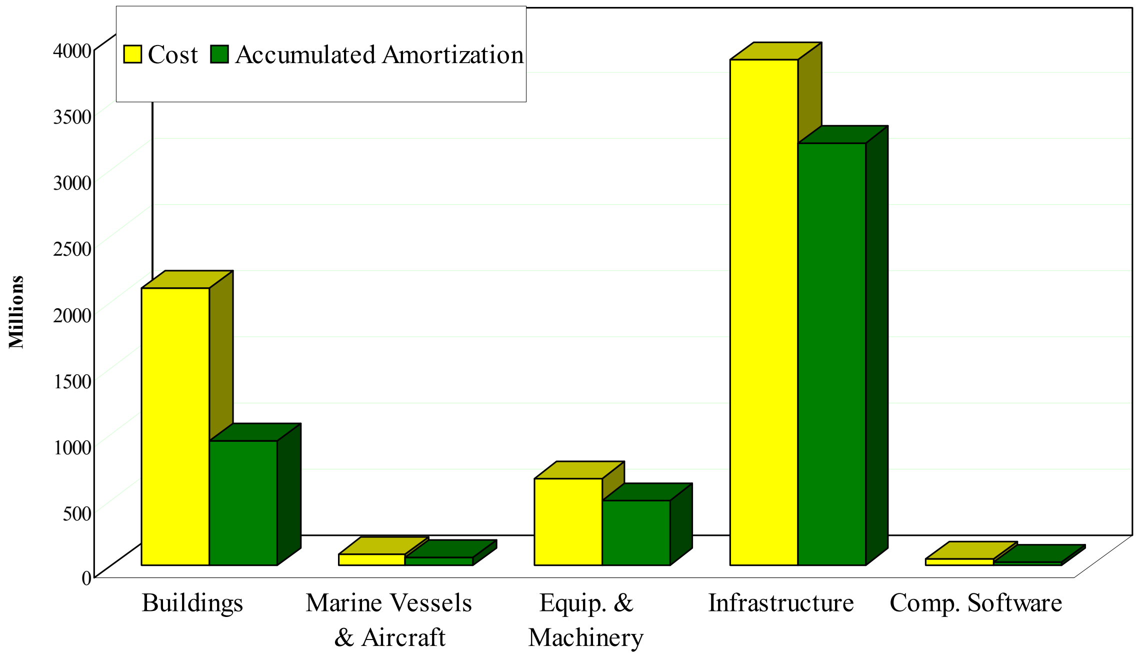
- The net book value of tangible capital assets declined by $44.1 million as acquisitions decreased overall and accumulated amortization continued to increase.

- The average accumulated amortization of tangible capital assets is 69.4%. 45.0% of buildings and 83.3% of infrastructure assets are amortized.

- The Province faces widely acknowledged significant challenges for investing adequately in public infrastructure. As shown by the graph, the Province's $3.8 billion investment in infrastructure (as defined above) is almost at the end of its useful life. Existing assets are depreciating at a rate greater than acquisition.

- Government is aware of the past reduced level of investment in marine vessels and aircraft, which are now 76.8% amortized, and has undertaken plans for strategic investments in marine vessels.

- 66.0% of computer software assets are amortized. However, during 2005, Government created the Office of the Chief Information Officer, established to bring a new focus for modernizing and improving information technology functions, including operational improvements and assets.



FINANCIAL POSITION

Net debt and accumulated deficit are comprised of the following components:

($ billions)	2005	2004	2003	2002	2001
Unfunded Pension Liability	3.93	3.75	3.56	3.39	3.35
Borrowings (net of sinking funds)	6.94	6.78	6.41	6.15	5.81
Group Health and Life Insurance Retirement Benefits	1.16	1.07	0.98	Note	Note
Other Liabilities	1.70	1.29	1.18	1.12	0.99
Less: Total Financial Assets	(1.84)	(1.40)	(1.51)	(1.73)	(1.71)
Net Debt	11.89	11.49	10.62	8.93	8.44
Less: Tangible Capital Assets	(2.08)	(2.13)	(2.13)	Note	Note
Less: Other Non-financial Assets	(0.06)	(0.05)	(0.05)	Note	Note
Accumulated Deficit	9.75	9.31	8.44	Note	Note

NOTE:
Prior to 2004, the Province did not recognize non-financial assets or group health and life insurance retirement benefits in its financial statements. Pursuant to direction from the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants, these items were recognized in 2004, with restatement for 2003. Accordingly, this information is not available for years prior to 2003.

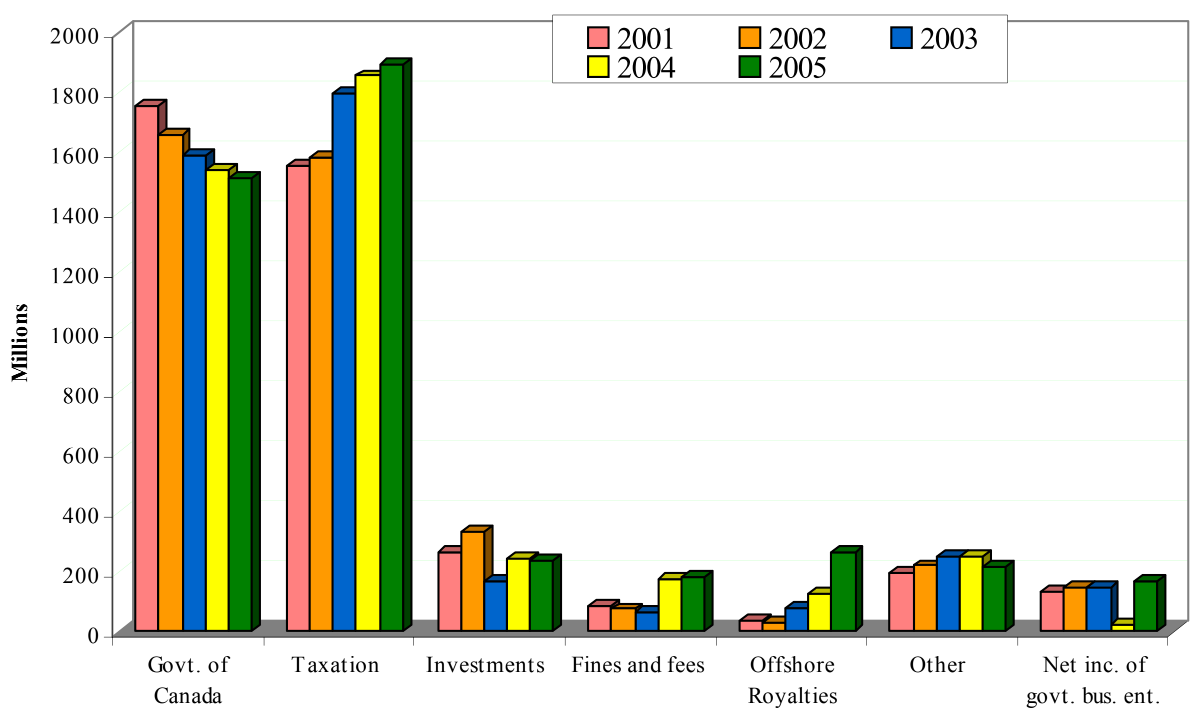
As seen in the previous chart, liabilities including net debt have been growing over the past five years, indicating that the Province still has significant financial challenges to face, in particular the unfunded pension liability.

HIGHLIGHTS - FINANCIAL OPERATIONS

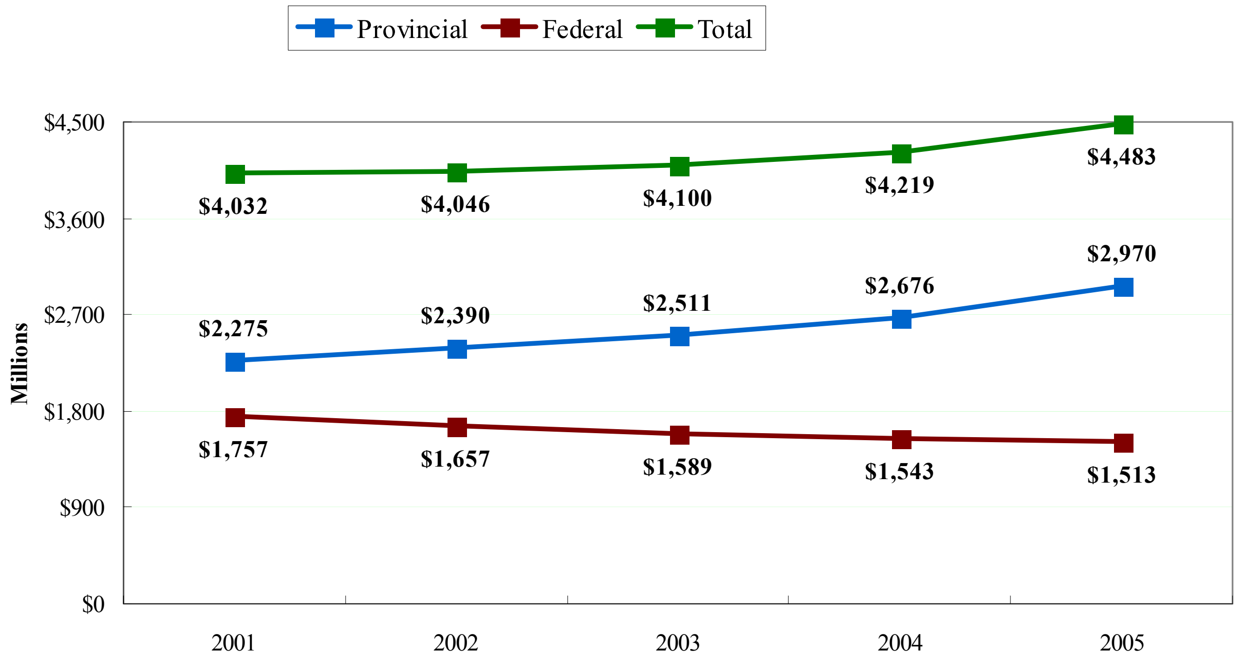
Revenues

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 - 5 Year Comparison*



b) ***Total Revenues - 5 Year Comparison***



From an analysis of the above charts and the information presented in the consolidated summary financial statements, 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, increasing steadily over the past five years to a high of $1.89 billion in 2005, an increase of $36.4 million from 2004.

c) ***Revenues by Source***

The most significant changes in revenues by source between 2004 and 2005 arise from offshore royalties and government business enterprises.

- In 2004, the net income of Newfoundland and Labrador Hydro decreased due to a write-down of capital assets in the amount of $130.9 million (net impact after minority interest - $118.6 million). Net income for 2005 has reverted to a rate comparable to previous years before the one time write-down, the primary reason for the $141.8 million change in net income of Newfoundland and Labrador Hydro for 2005 over 2004.

- Offshore royalties increased by $137.9 million, or 108.7%, between 2004 and 2005. This is primarily due to higher than usual oil prices and increased production.

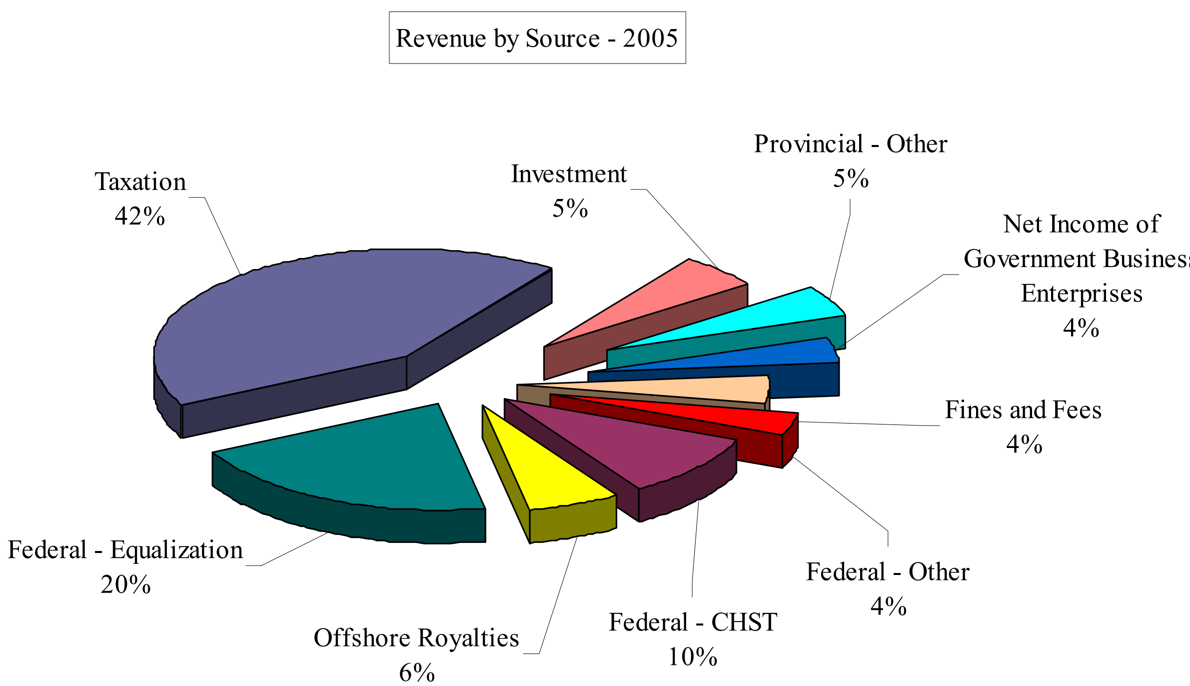
- A gradual decline in Government of Canada revenues continues to impact on overall revenues.

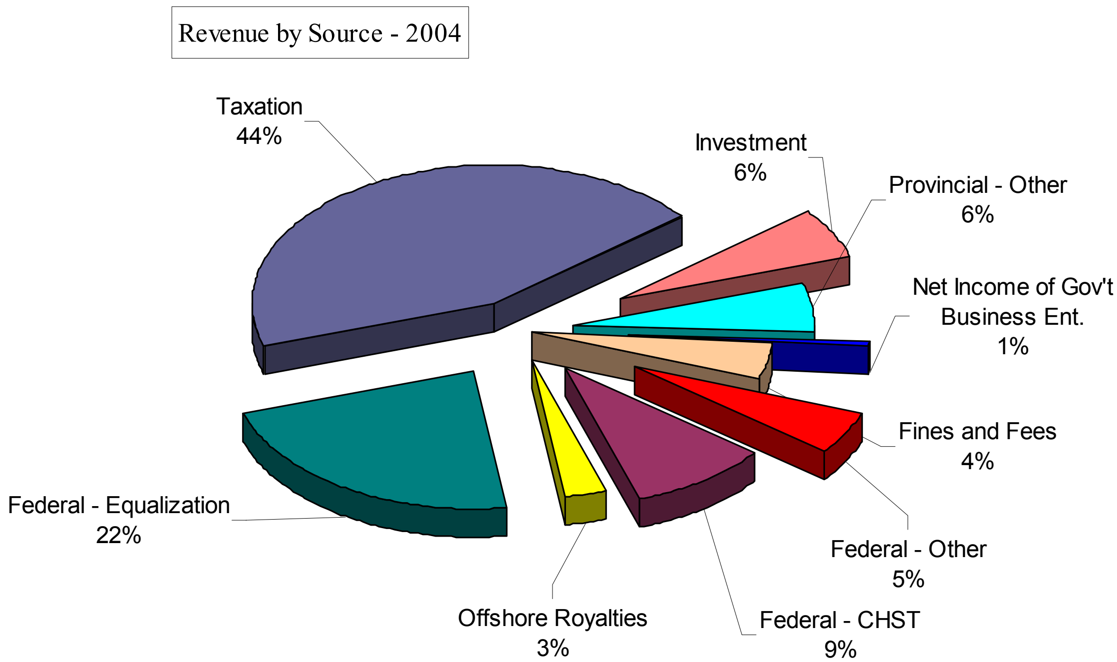
The following charts depict revenues by source for the current and preceding years for comparative purposes.

- 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.

- Personal income tax remains the second most significant source of revenue in 2005, representing 17.1% of all revenues (marginally higher than the 2004 rate of 17.4%) and 25.8% of all provincial revenues.

- As stated earlier, taxation is the most significant source of revenues overall although taxation as a percentage of all revenues decreased slightly to 42.2% in 2005 from 44.00% in 2004.

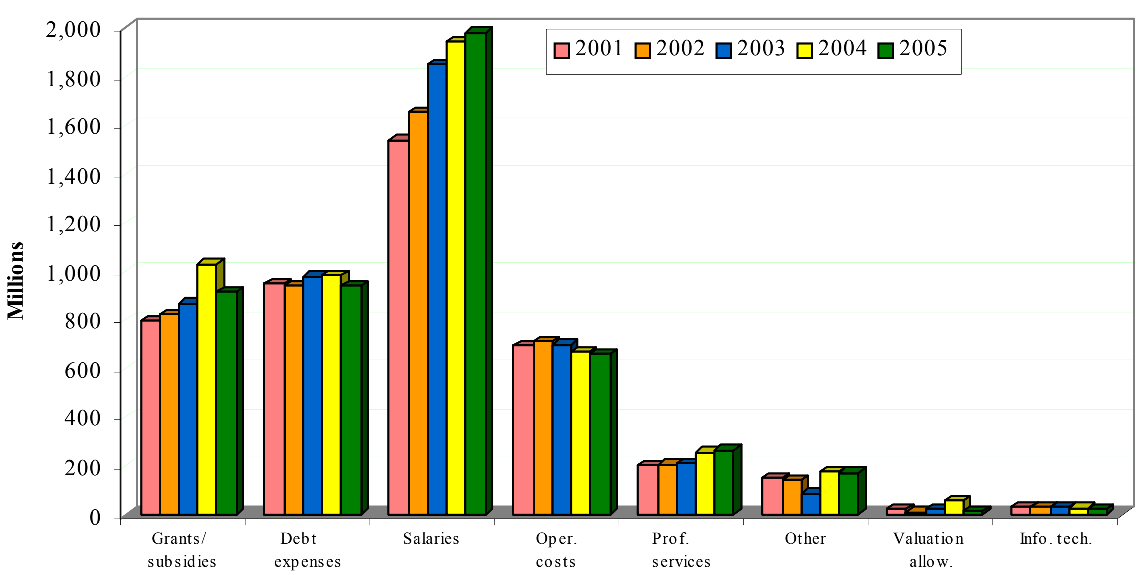




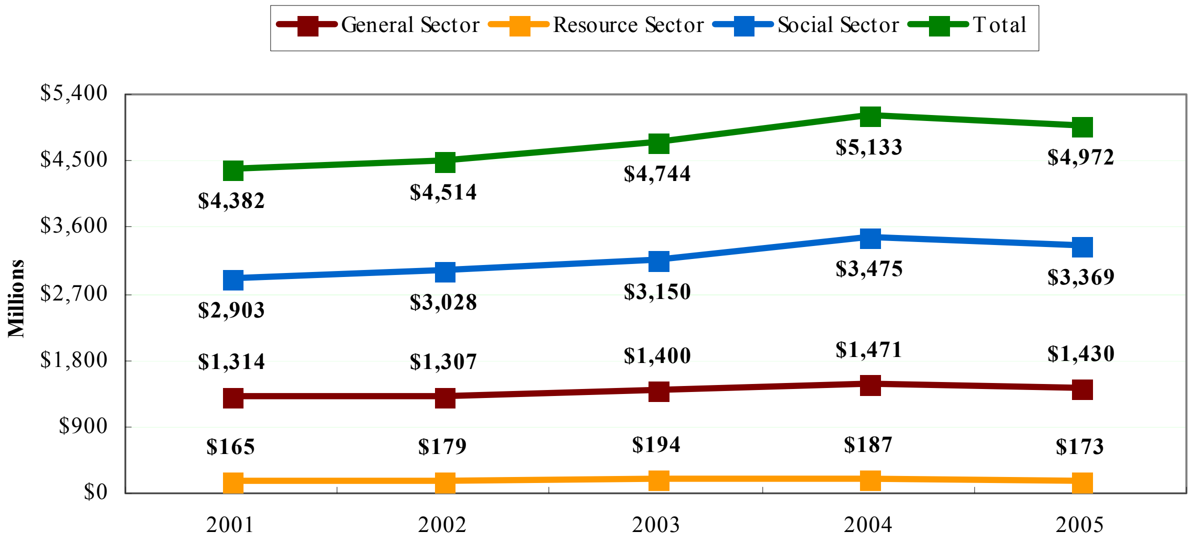
Expenses

For 2005, total expenses amounted to $5.0 billion. The following charts and discussion analyse 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. However, this category does not include amortization expense and loss on sale relating to tangible capital assets for fiscal years prior to 2003 due to the accounting policy change applied to subsequent fiscal years (see note on page 12).

a) *Expenses by Major Category - 5 Year Comparison*



b) ***Expenses by Sector - 5 Year Comparison***



From an analysis of the previous charts and the information presented in the consolidated summary financial statements, the following observations can be made:

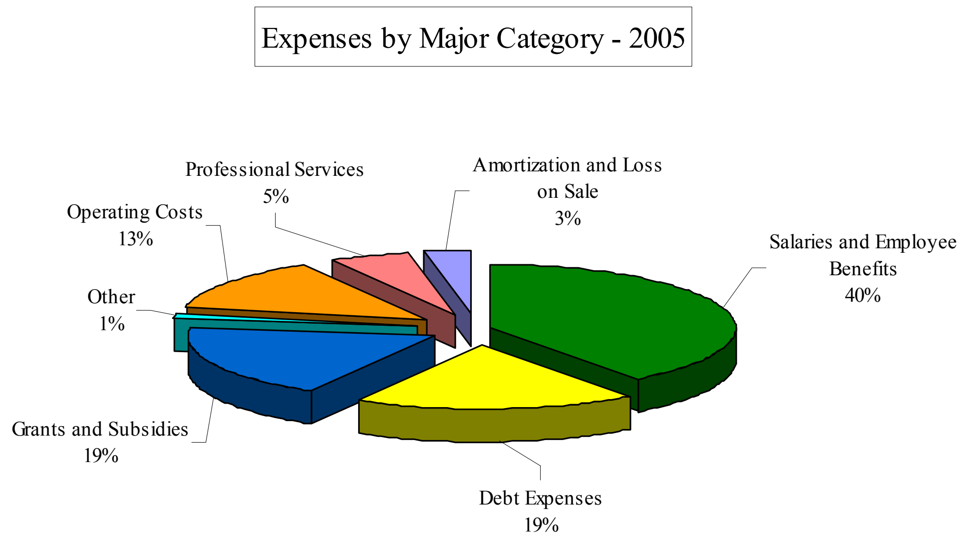
- Total expenses increased by $751.3 million from 2001 to 2004, then decreased by $160.6 million to 2005, representing a change of 3.1% from 2004.

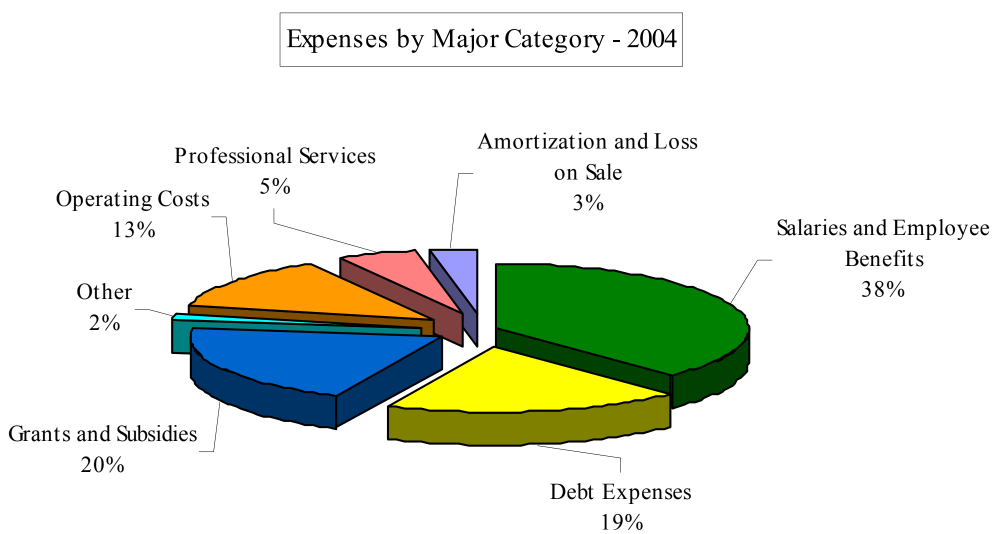
- Salaries and employee benefits remain the most significant expense, increasing steadily over the past five years from $1.5 billion in 2001 to $2.0 billion in 2005; an overall increase of $440.7 million in those five years, or 2.0% from 2004 to 2005.

- 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.

c) *Expenses by Category*





The most significant changes in expenses by category between 2004 and 2005 relate to decreases in grants and subsidies, debt expenses and valuation allowances.

- Grants and subsidies expense decreased by $112.8 million between 2004 and 2005. This can be partially attributed to a $14.4 million reduction in municipal grants for debt charges, $11.6 million less required for disaster assistance, and another $7.8 million decrease in other municipality-related expenses. A $5 million one-time debt repayment in 2004 and other lower than usual expenses of $5.4 million related to the winding down of several federal - provincial agreements contributed to the variance.

- The majority of debt expense relates to the Consolidated Revenue Fund for interest on debt, foreign exchange amortization/losses and interest on the unfunded pension liability. Part of the decrease of $41.2 million between 2004 and 2005 can be attributed to lower interest rates on refinanced debt, and a stronger Canadian dollar which reduced the cost of servicing foreign debt. There is a decrease in realized foreign exchange losses of $52.5 million as no foreign denominated debt was redeemed in 2005. Offsetting this decrease is a $17.1 million increase in amortization expense on debenture debt as a result of foreign exchange losses of past years.

- Valuation allowances decreased by $43.3 million between 2004 and 2005. An overall change in bad debt expense for the Newfoundland and Labrador Student Loan Corporation accounts for $20.4 million of this decline, while a decrease in bad debt expenses for the Consolidated Revenue Fund accounts for an additional $24.6 million. A government-wide review of provisions for bad debt expense in 2004 resulted in a more appropriate valuation of these provisions, contributing to the lower bad debt expense in 2005.

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 primarily 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 public sector 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:

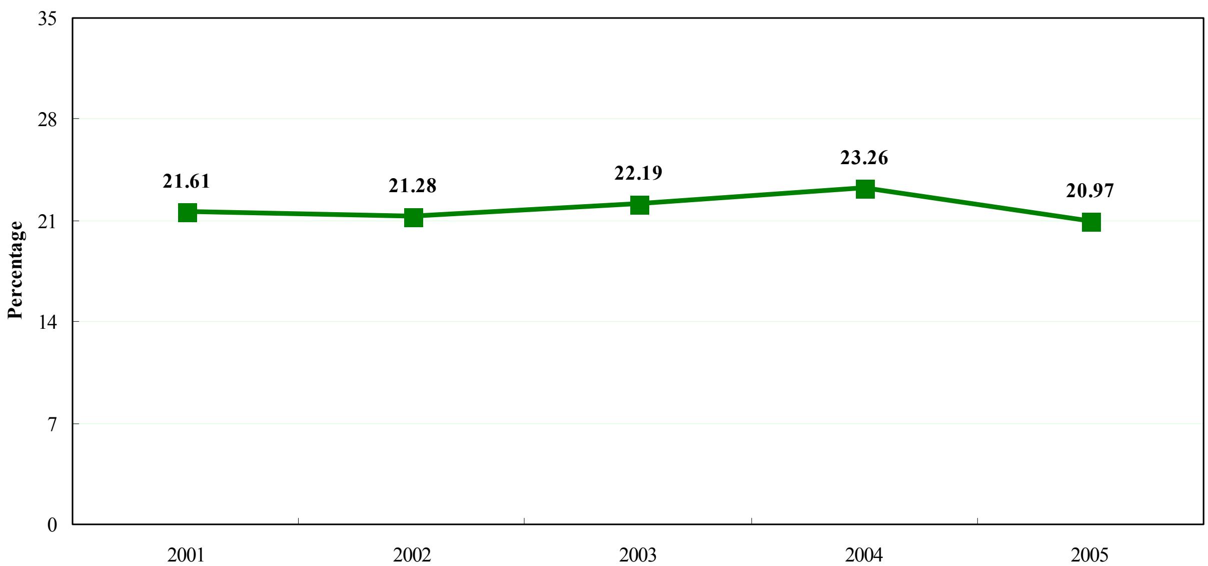
a) *Province's Interest Cost as a Percentage of Revenues*

- 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 financial statement discussion and analysis. For the purpose of this analysis, the expenses have been restated for the past five years.

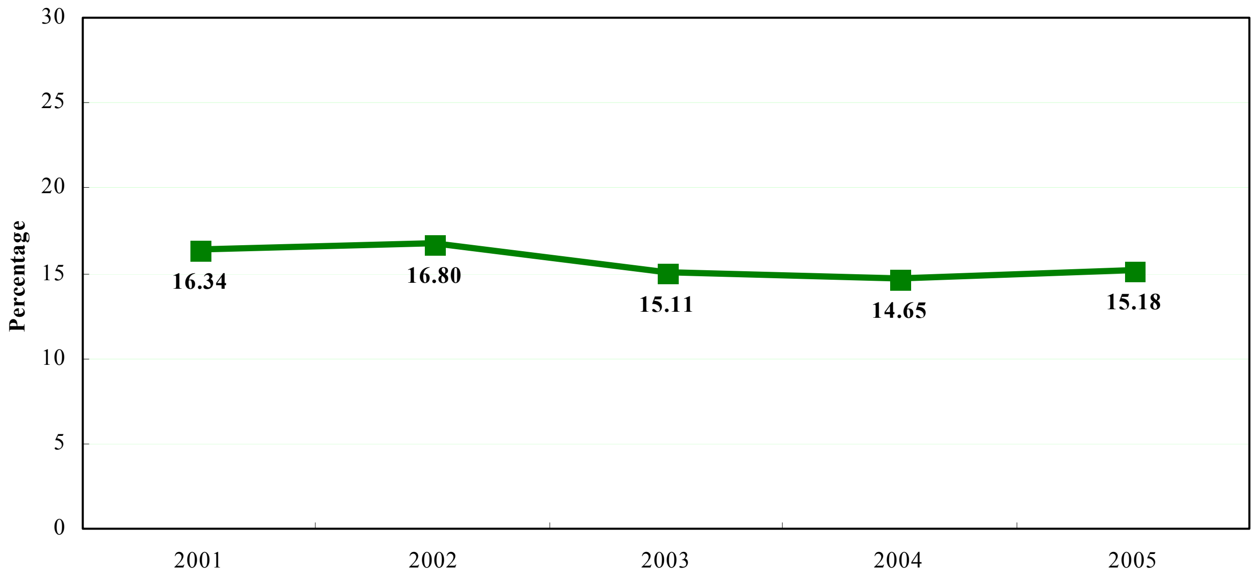


b) *Provincial Revenues as a Percentage of GDP*

- 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.

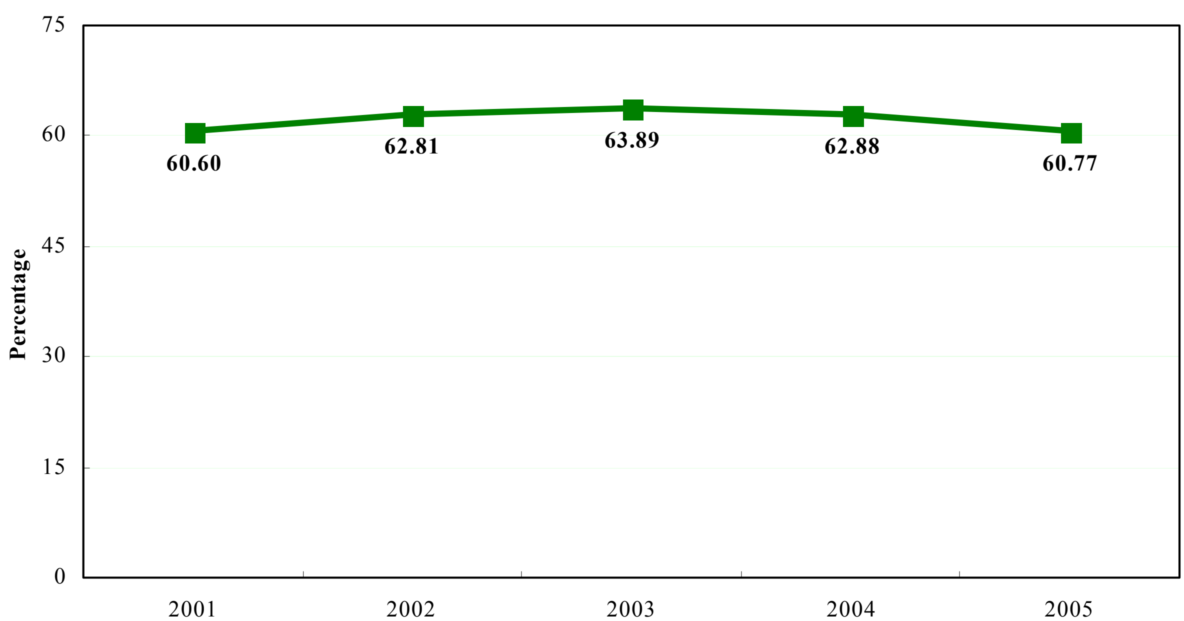


Sustainability

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 preceding 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 manoeuver in making fiscal choices.

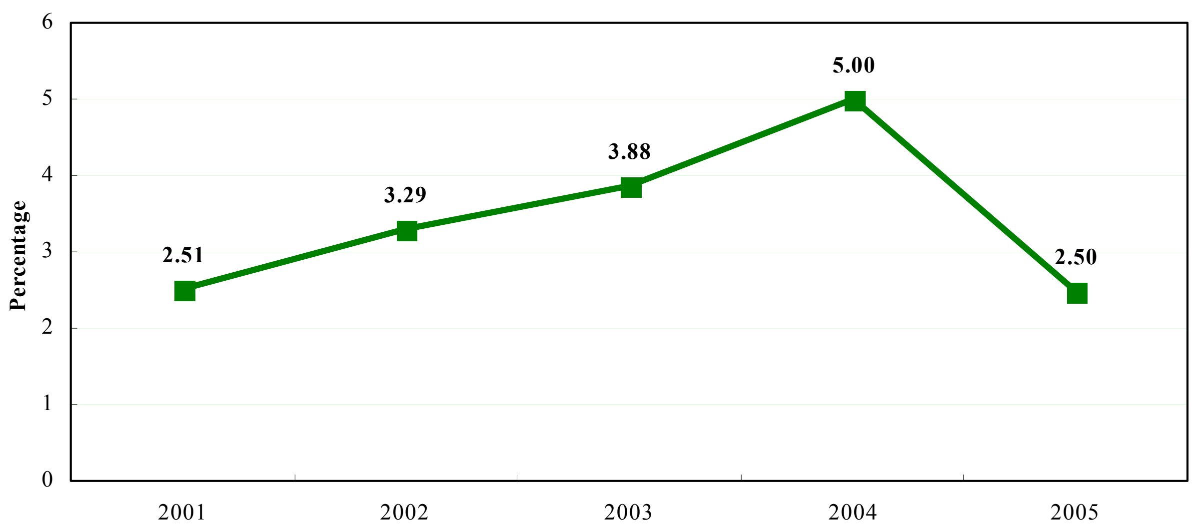
- The average of this ratio over the past five years is 62.19%, with a slight decline from 62.88% in 2004 to 60.77% in 2005.

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 graph below, 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.

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

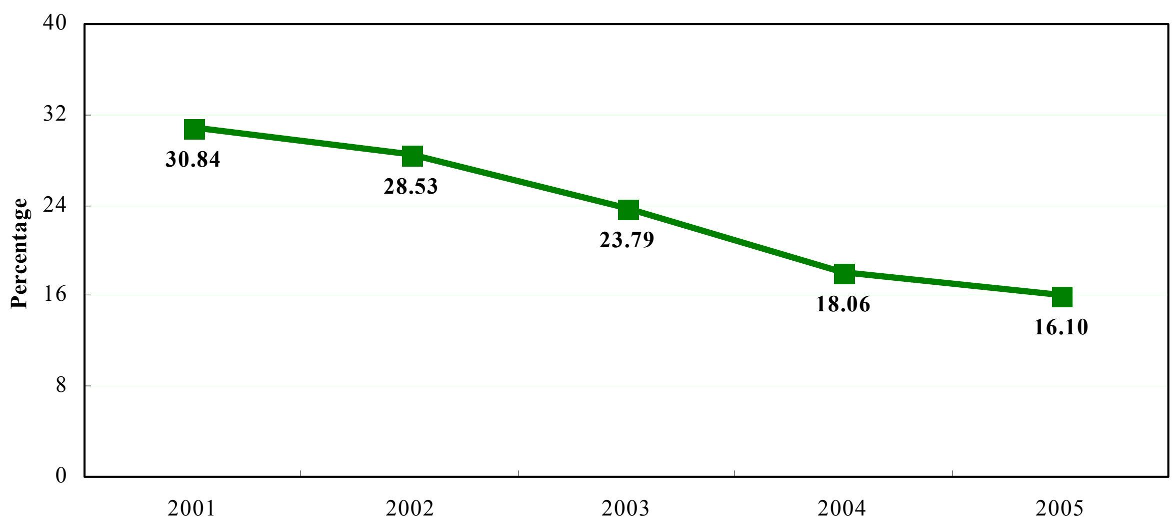


Vulnerability

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*

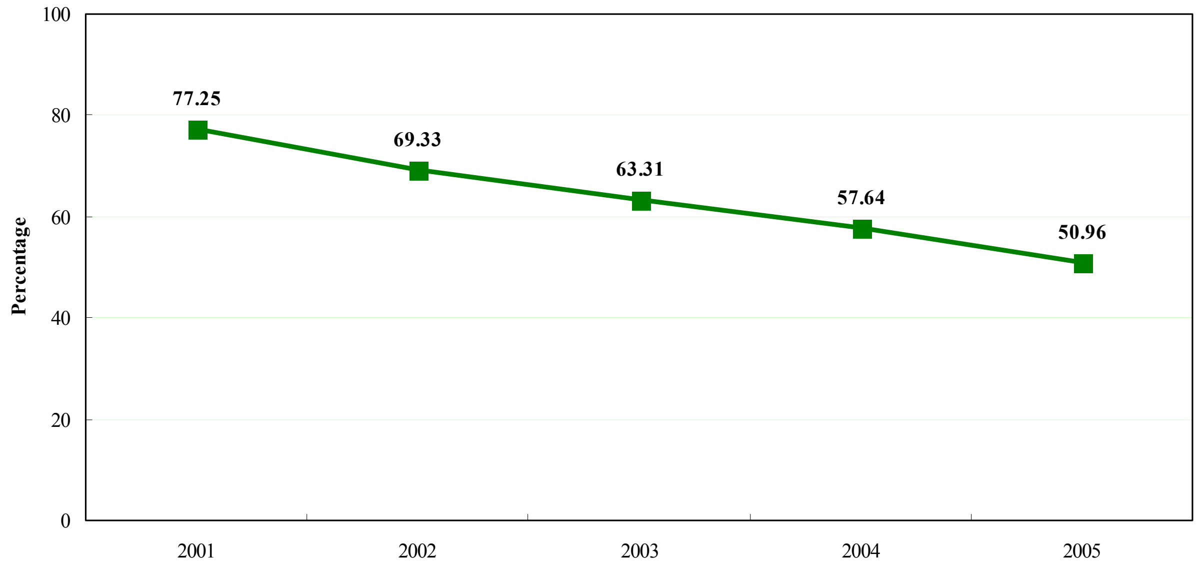
- This ratio measures the Province's foreign currency debt relative to its net borrowings. It reflects the degree of vulnerability to foreign currency swings that the Province faces.
- As indicated in the following graph, foreign currency debt as a percentage of net borrowings has decreased steadily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



FINANCIAL PERFORMANCE

The fiscal policies and deficit reduction measures introduced in Budget 2004 for the fiscal year ended 31 March 2005 were intended to ensure fiscal stability and sustainability by focusing on responsible spending controls while maintaining strong, economic growth. The discussion and analysis presented in this report clearly indicate that Government is on track to meet long term objectives for restoring the financial health of the Province. Other financial indicators including net debt, accumulated deficit and net borrowings have increased, but at a significantly lower rate than in the previous four years, indicating an overall improvement in financial performance.

Newfoundland and Labrador is in a better position than at the beginning of the 2004-05 fiscal year. Measures have been implemented to contribute to a deficit reduction strategy over the next few years while the new Health Accord and the Atlantic Accord (2005), a newly negotiated arrangement on the sharing of offshore petroleum revenue, will enhance the Province's long term financial circumstances. Government's challenge will be to remain vigilant in managing the Province's financial position while maintaining social and other responsibilities.