

Prince Edward Island

2002 Budget

A Balanced Response to Difficult Times

**Presented to
The Members of the Legislative Assembly of Prince Edward Island**

by

Honourable Patricia J. Mella

**Provincial Treasurer
and
Chair of Treasury Board**

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<http://www.gov.pe.ca/budget/>

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PRINCE EDWARD ISLAND 2002 BUDGET

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THE BUDGET ADDRESS

A Balanced Response to Difficult Times

Madam Speaker, Members of the Legislative Assembly.

A year ago I presented the 2001 Budget the theme of which was *Keeping the Balance in Uncertain Times*. At that time there were troubling signs that the strong economic growth Canada had been enjoying in previous years was coming to an end. I noted that, "The distinct slowdown in the US economy, coupled with severe reductions in world stock markets have caused a serious reassessment of the economy."

Madam Speaker, using the best information available at that time we developed our Budget, predicated on this uncertain economic outlook. But no one could have foreseen the tragedy that overtook the world on September 11, 2001. This heinous act of terrorism went beyond all known bounds of humanity.

Casting our thoughts back to the events of that day and the months following, let us not forget the uncertainties and impacts resulting from:

- C one, the immediate closure of airspace to the US and diversion of traffic to Canadian terminals;
- C two, the obstruction to trade across the US border;
- C three, the demands for and response to the need for increased security at airports and strengthened border controls;
- C four, the decisions to target military forces on Afghanistan; and
- C five, the uncertainty surrounding the success of these measures.

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It now looks as though the direct threat that was posed to our society has been successfully countered, although the effort continues. Also, the latest news points to encouraging signs that the North American economy is improving. However, the events of September 11 caused an immediate loss of air travel and a drop in business and consumer confidence. In the months following, the global economic climate became very clouded.

Public Input

Madam Speaker, this has been a challenging Budget to prepare. I have, however, been helped in this task first, by my colleagues and second, by the advice of those who wrote and spoke to me during its preparation. As in previous years I invited members of the public and interest groups to advise me on their priorities, concerns and thoughts on the Budget. I am always encouraged by the interest demonstrated by many in the finances of the Province and their concern for the economic future of Prince Edward Island.

We listen and learn from all the advice from every quarter concerning the Budget.

Madam Speaker, budgets are inherently about the efficient and effective use of the taxpayers' hard-earned dollars and as such they must reflect the needs of the people of the Province.

I must point out, however, that there are large elements of our fiscal situation that are beyond our control. Approximately 40 per cent of our revenues come from federal sources and hinge on the national economy, coupled with decisions and actions of the Federal Government. I will speak more of this later, but it will become evident through this discourse that the uncertainties surrounding federal transfers are the main reasons why this Budget has been so challenging.

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Economic and Fiscal Performance

Last year's Budget anticipated that the Canadian and Provincial economies would grow more slowly in 2001 compared to previous years. In fact, the GDP for Canada in 2001 expanded by only 1.5 per cent in constant dollars, compared to 4.4 per cent in the previous year. For Prince Edward Island we estimated growth of 1.3 per cent in 2001, which compares to 3.0 per cent in the previous year. The reduced pace of economic growth also slowed employment gains from the record 5.2 per cent increase we enjoyed in 2000, to 2.2 per cent in 2001.

Madam Speaker, I am happy to be able to report that notwithstanding the slower pace of growth, there were approximately 66,000 Islanders employed in 2001, which is an all time high. The expansion in employment meant that an additional 1,400 persons were working last year. Unemployment fell to a low of 10.2 per cent in June 2001 resulting in an annual average of 11.9 per cent, the lowest since 1981.

Nationally, the slowing economy prompted the Bank of Canada to lower interest rates ten times from a high of 6 per cent to 2.25 per cent. By year's end interest rates were at their lowest in 40 years. This aggressive reduction in interest rates encouraged a sharp increase in consumer spending, with car sales being a major contributor. Further, during 2001 energy costs fell sharply, following their escalation last year.

Reflecting on the economic performance of the Province during 2001, it may be recalled that our main concern at the outset of the year was the embargo on potato shipments to the United States. Working closely with the potato industry, the Province showed its determination to prove that the potato wart problem was isolated and we pressed the Federal Government to negotiate with the US Government to lift the embargo on shipments. Thanks to these efforts, our farmers were

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Island farmers faced another serious problem in the subsequent crop year as near-drought conditions in the growing season resulted in a very small harvest, particularly the potato crop. The volume of potatoes was 39 per cent below the 2000 crop. This in turn caused potato processors to reduce the level of their production. Fortunately, improved potato prices, combined with the support programs provided by the federal and provincial governments to potato farmers in early 2001, permitted farm cash receipts to expand to \$335.6 million in 2001, up from 2000 by 4.3 per cent.

The trade embargo hurt our exports, which were down by 3.7 per cent in 2001, following dramatic growth in previous years. Tourism did relatively well in 2001 going against the regional trend, with \$310 million of expenditures, up by 10.7 per cent from last year.

Lobster landings reached \$100 million in 2001, an all time high, although we did note that fish volumes were down somewhat.

Retail sales reached a record level of \$1.3 billion, expanding by 3.9 per cent from the previous year. This was aided by the extremely low interest rates.

Madam Speaker, insofar as the provincial economy goes, our forecast for 2001 at Budget time now appears to be reasonably on target.

A fuller explanation of the economy is contained in Budget Paper A. I will now turn to the fiscal outcome for the year 2001-2002.

Madam Speaker, the budgeted revenues for 2001-2002 were forecast to expand by only 1 per cent from their forecast levels of 2000-01. I am happy to report that revenues in total have exceeded budget by \$14.5 million.

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In the 2001 Budget we had estimated that our own source revenues would be \$545.8 million in 2001-2002. These are revenues that are derived from provincial taxes and other local sources. At \$549.9 million, they are essentially on target.

Madam Speaker, the Federal Government provides provinces with revised estimates of their equalization entitlements twice a year. These federal estimates fluctuate widely from estimate to estimate with the result that we have learned to use our own information in an effort to more reliably predict our revenues and plan for the future. Only as recently as February 28, 2002 we were informed of significant differences in the previous numbers the Federal Government provided which contrasted with our forecast revenues. As it now stands, our original estimates are off by only 2.6 per cent.

On the expenditure side of the account, our Government made it clear in late 2001 that efforts were needed to reduce the pace of spending, in light of the evident slow growth in revenues. Following the second quarter review, line departments responded by reducing spending by \$11 million. We also put in place a policy to freeze hiring with exceptions for hiring for essential services only.

Expenditures are now forecast to be \$986.7 million, which exceed the original Budget by 2.8 per cent. I might add that this represents an increase of only 2.4 per cent from the spending limits in the previous year. Part of this increased spending is the result of the acceleration of the East Prince Health Facility construction.

In view of the additional work on the Health Facility, involving \$19.4 million of expenditures in 2001-2002, the overall forecast is a deficit of \$14.5 million. I am happy to report that, exclusive of the Province's investment in the East Prince Health Facility, the projected surplus for 2001-2002 is \$4.9 million. This compares to a budgeted surplus of \$11.6 million for the year. The difference of \$6.7 million represents less than 1 per cent of our total budget.

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Madam Speaker, I can assure you that this Government has been vigilant in its efforts to keep the lid on spending and in any other year the limited expenditure expansion that was allowed would have resulted in large surpluses. Additional investments were provided for priority reasons only.

What are these priority areas? Government's priorities are the priorities of Islanders. Health costs are higher than Budget by \$13.8 million, largely in view of the work on the East Prince Health Facility which, as I noted, is moving ahead faster than had been anticipated.

The Province acted on an opportunity to assist in a substantial expansion of the aerospace sector in Slemon Park, increased funding of \$500,000 for Tourism Marketing and completed additional highway maintenance. Further, we also had to deal with the unanticipated School Boards deficits of \$1,080,000.

Madam Speaker, this was the nature of our additional spending in 2001-2002. I would like to emphasize that when we complete our budget, we make our best estimates based on all available information. Actual results will vary from these estimates depending on events and circumstances that occur throughout the year. Variances from budget are not unusual and in fact can be expected.

Economic Outlook

I should now like to turn our attention to the future.

Fortunately, there are some preliminary indications that the economic slump may have bottomed out. The latest economic statistics on the American and Canadian GDP indicate that the fourth quarter was not as weak as had been initially anticipated. More recently, the Governor of the Bank of Canada declared that the recovery is underway.

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Madam Speaker, it would be imprudent to budget in anticipation of a major economic improvement in view of the present uncertainties. We hope that there will be progressively better news on the economy as the year unfolds, but the strength of the recovery is still the subject of speculation at the moment.

The December 2001 Federal Budget forecast that the national economy would expand by 1.1 per cent in 2002 and 3.9 per cent in 2003, following growth of only 1.5 per cent last year. For Prince Edward Island our forecast is for the economy to grow by about 1.2 per cent this year.

The important point to bear in mind is that growth rates in 2001 and 2002 are very modest by comparison to the pace of growth that we had been experiencing from 1996 to 2000. I might note that as recently as October 2000 the Federal Government was anticipating sustained economic expansion of 3 to 3.5 per cent per year in 2001 and 2002. The fiscal consequence of the reduced rate of economic expansion means that our flexibility in 2002 is somewhat compromised.

Fiscal Outlook

Madam Speaker, we now believe that the slow level of revenue growth that occurred in 2001-2002 will turn into a decline in 2002-2003, with resulting difficult fiscal consequences. The Budget for 2003 shows that revenues will be less than the previous year by \$3.8 million.

The main reason for this situation is a decline of federal revenues by \$34 million in 2003, from our forecast revenues in 2002.

By contrast, our own-sourced revenues, generated from the taxes we receive on sales, personal income and property are expected to grow

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Federal revenue performance is weak for a variety of reasons, and there is added uncertainty in the coming year over exactly what can be expected.

Madam Speaker, Members may recall that in January of this year provinces were unexpectedly informed of the misallocation of federal income tax to some provinces that resulted from a federal accounting error in the administration of capital gains tax from Mutual Fund Trusts. We were informed that this resulted in an estimated overpayment of Equalization to us of some \$6 million. Madam Speaker, we still have received no indication of how this will impact on our Equalization in the coming year. In the 2001 Federal Budget the Government of Canada committed \$2 billion to an infrastructure program. Madam Speaker, we still have no information on how this is to be distributed although we are committed to working with our federal counterparts. Most of our regional economic development agreements have now expired, but Madam Speaker, we still do not know when and by how much they will be renewed.

The population numbers from the 2001 Census have just been released, and Madam Speaker, they also have potentially large impacts on major federal transfers.

On top of these challenges, all provinces continue to have serious disagreements with our federal friends over the ceiling on Equalization and the inadequacy of the CHST transfer. I should note that in 2001 I appeared before both the House of Commons Finance Committee and the Senate Finance Committee to explain why the Equalization program is deficient. All Provincial Premiers and Ministers of Finance have called on the Federal Government to remove the ceiling on Equalization and to strengthen the program, and to raise their transfers in support of Health, Education and Social Services, through the CHST transfer.

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More details on these concerns can be found in Budget Paper B.

Madam Speaker, our CHST cash in 2002-2003 will be about \$89 million which is an increase of approximately 2.8 per cent over last year, however, our expenditures on health are growing in excess of 7 per cent per year. CHST funding is still below the level of support we received some eight years ago in 1994-95. We estimate that our Equalization payments will be considerably below their 2001-2002 level and that calculation is highly uncertain. Still, the Federal Government insists on applying a ceiling to payments. In addition, other federal transfers are clouded in uncertainty.

Madam Speaker, I trust that Members of this House and the public will understand the issues that confront the Government in the preparation of this most challenging Budget.

The Year Ahead

In view of the weak revenue picture for 2002-2003 we must budget prudently while maintaining our commitments. Although we will depart from our goal of a balanced budget for 2003, we have every expectation to return to a balanced situation in 2004.

As we announced earlier this year, when we began the Budget exercise we realized that the shortfall in revenues and the underlying growth in expenditures created a projected deficit of an unacceptable level. This was our starting position.

Through the course of developing this Budget we have acted to pare down spending drastically. In the course of the Budget exercise we adhered to the principle that delivery of essential services will continue, and that we recognize our responsibility to our employees and will honour the salary settlements established through contract negotiations recently concluded.

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In responding to the challenge of the difficult times, we have set overall spending in 2002-2003 at a level only 1.4 per cent higher than the forecasted expenditures of the previous year.

The overall excess of revenues and expenditures in the coming fiscal year will produce a deficit of \$11.6 million before the Province's investment in the East Prince Health Facility and a deficit of \$28.8 million subsequent to the investment. Madam Speaker and Members of this House, this represents a significant improvement from the deficit that we faced at the start of the Budget exercise. Generally, governments will run deficits during economic slowdowns because revenues are lower than normal. When this occurs, it is referred to as a cyclical deficit which governments believe will be eliminated as economic conditions improve.

Tax Measures

Madam Speaker, we have resisted general tax increases with the exception of two tax measures which I will announce in this Budget.

As of midnight tonight, the Health Tax will be raised by \$5 per carton of 200 cigarettes and proportionate increases will be raised on related tobacco products.

This measure follows similar steps in other provinces, the primary aim of which is to act as a further disincentive to smoking. Prince Edward Island will be among the forefront of provinces aggressively acting on cigarette smoking as we previously raised the tax in April and December of last year.

The tax on gasoline will increase by 1 cent per litre as of midnight tonight. An analysis of the most recent prices across Canada shows Prince Edward Island prices to be among the lowest in Canada, lower

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than the Canadian average and the lowest in Atlantic Canada.

Priorities for 2002-2003

Madam Speaker, few could disagree that the development of this Budget was undertaken in an extraordinary period of global uncertainty.

Notwithstanding the problems that beset the economy, the most difficult aspect of this has been the volatile nature of the revenues delivered through the federal system. This not only includes Equalization and CHST but also the federal share of development funds, infrastructure monies and the Personal and Corporate Income Tax, all of which are administered federally. The ability of the federal system to provide reliable and accurate forecasts of our receipts is sadly lacking.

Bearing in mind the overall revenue decline within which we are working in 2002-2003, some reductions in spending have been necessary.

Overall, expenditures have been reduced by \$39.5 million in 2002-2003 from the Status Quo Budget. This represents a reduction of 4 per cent in overall spending. The reductions come from a wide variety of programs and services across all departments.

The largest reduction is in our Highways Budget from which \$12.5 million in planned capital spending has been delayed.

The second most significant reduction is in the Education Capital Budget, which is reduced by \$5.2 million. The construction of the Summerside Intermediate and Bluefield Phase II schools will be delayed, however, our Government is committed to the completion of these projects as soon as revenues permit. I must emphasize, however, that other school construction programs will proceed as

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planned. The Kinkora School is proceeding as scheduled. I should note that we have already completed the Parkdale School addition, the Summerside/Miscouche French School and the West Prince French School. The Miscouche Consolidated School addition project is also well underway.

We are holding fast to our commitment to bring MRI and Linear Accelerator services to the Province. Our Government will make investments of \$9.6 million in the fiscal year to support their capital costs as well as \$1.6 million to fund the start up costs of these important services. We have already recruited a highly respected radiation oncologist to develop this much needed service.

We will also begin the planned expansion of the O'Leary Community Hospital, budgeted at \$1.1 million this year.

We have introduced a voluntary workforce adjustment program in an effort to reduce costs and streamline the delivery of services. The projected savings of \$3.75 million will assist in the renewal of the Provincial Government workforce.

Madam Speaker, I could go on and provide more details of the reductions to our spending plans that were necessary this year but would prefer to leave this to the respective departmental Ministers who are more knowledgeable than I am on their programs.

Improved Services

Madam Speaker, I would like to discuss the large improvements in our public service that our Government continues to achieve.

Last year more than 45 new registered nurses began work here. Overall we now have 1,411 nurses, compared to 1,364 a year ago. We were able to recruit 8 family physicians and 12 specialists. During 2001, each of our Health Regions were awarded maximum

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accreditation status by the Canadian Council on Health Services Accreditation. We have provided an additional \$2 million to provincial drug programs, largely the Seniors and Financial Assistance Program. We have increased funding to private nursing homes over the past four years and will increase funding by a further \$480,000 in 2002-2003.

An additional \$1.5 million is provided to home and palliative care, and a further \$1.5 million for the Disability Supports Program.

Madam Speaker, the Government is resolute in its desire to carry forward its commitments despite the difficult financial pressures that exist. The largest investment in 2002-2003 is the East Prince Health Facility whose pace of construction is ahead of schedule. We have budgeted \$21 million for this project, which we now expect to be near completion by April 2003.

Education and training are the cornerstones of the future development of the Province. Our Government has maintained 33 teaching positions despite declining enrollments. During 2001-2002, initiatives were taken to improve literacy in both French and English. Last year was the second year of the publicly-funded community based kindergarten program. Significant investments were made by the Province to support facilities and students at Holland College, UPEI, the Atlantic Veterinary College, and the UPEI School of Nursing. This Budget allows for those continued investments.

Madam Speaker, the agriculture and food industry of the 21st century will be transformed significantly by ongoing developments in science and technology, the adoption of new economic opportunities from innovative agriculturally-based products, and growing consumer demand for safe, high quality products produced in an environmentally responsible manner. Helping new and existing producers acquire the skills, knowledge and tools they need is a priority of this Government.

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FarmNet, a new web-based service, is being developed with the involvement of all sectors of the industry as a long-term, broad-based and multi-faceted approach to connectivity, skills development and for integrating information and communication technology into new and existing farm business practices.

Over the past three years under the Agriculture and Environmental Resources Conservation program, a total of upwards of \$6.5 million was provided for on-farm conservation projects. Given the success of this three-year initiative, a new program will be developed to improve the sustainability and productivity of agricultural operations.

The Department of Agriculture and Forestry is also working with several interested organizations to examine options for a Model Forest program for Prince Edward which would bring people together to create a shared vision for Island forests and develop strategies to enhance the many timber and non-timber benefits they provide. To this end, the Department is also working closely with the Public Forest Council to increase awareness of the Island's public forest lands and the non-timber potential of these lands.

Madam Speaker, our drinking water is one of our most precious assets. Last year we committed \$270,000 to a long-term Drinking Water Strategy. This year we are committing \$382,000 to protect our water for present and future generations.

The Province will sustain its commitment of \$250,000 per year to the Lobster Science Centre at the Atlantic Veterinary College and provide additional resources for further research into this, one of our most important primary resources.

During 2002 the provincial Department of Fisheries, Aquaculture and Environment in partnership with the PEI Aquaculture Alliance and the Aquaculture Association of Canada, will host Aquaculture 2002, the largest annual event of its kind in Canada.

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Communities

Strong and vibrant communities contribute to the overall success of our Island economy. Our Government continues to promote and invest in economic initiatives to build and sustain our communities. Notre gouvernement continue à supporter et investir dans des initiatives économiques pour soutenir le développement de nos communautés. The Community Development Bureau will partner with Island communities to develop local projects.

Conclusion

Madam Speaker, the theme of this budget is “A Balanced Response to Difficult Times”. It is an honest assessment of the impact on the Province’s economy and fiscal position of the economic downturn that overtook the nation in 2001. It is a temporary but responsible departure from our long-standing goal of balancing our accounts, reducing taxes and lowering the debt.

The legacy we leave our children cannot be debt covered by deficits. We know we must invest in the future and not allow short-term challenges to take us from our long-term goals.

The future of Prince Edward Island is dependent on the dedicated people who share our commitment to make this province a better place to live.

This Budget keeps the Province on its course notwithstanding the difficult times that we are passing through.

Madam Speaker, we will continue to take a balanced approach and focus on clear public priorities which will lead to balanced results. I believe this budget clearly articulates that approach and focus.

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