Nova Scotia

Fiscal Overview

NOVA SCOTIA

2007

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Minister of Finance

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Introduction

The Province of Nova Scotia has seen improved fiscal performance in recent years. The government has introduced balanced budgets five years in a row and has generated surpluses at the end of each year.

Over the same period, the government has made significant additional investments in essential programs such as health care, education, and economic development, while tackling smaller but important emerging priorities such as health promotion and immigration.

This overall direction has been positive for Nova Scotians, and the results have been well received both inside and outside of the province. All three major bond-rating agencies have increased the province's credit ratings.

The government's goal for 2007–2008 is to build on these strengths to

- create winning conditions through a globally competitive business climate, workforce, and connections
- seize new economic opportunity by being a leader in information technology, research and development, innovation, and the clean and green economy
- support Nova Scotians in their efforts to become healthier and more active, in safe and accessible communities, neighbourhoods and workplaces

The province will pursue these goals in 2007–2008 amidst some challenging fiscal circumstances.

The Government of Canada has not yet provided a solution to the fiscal imbalance problem. Three national studies over the last year have acknowledged that small provinces like Nova Scotia do not have the capacity to fund expensive national programs like health care and education without additional assistance from the federal government. Yet federal figures released in late January indicate a decrease in Equalization payments for Nova Scotia for 2007–2008.

Nova Scotia is unlikely to find other revenue sources to offset slower growth in federal revenues. Nova Scotia tax levels are already among the highest in Canada, so any increase in taxes would further compromise our competitive position with other provinces and jurisdictions.

Another consideration is the downward trend in other revenue categories that may continue into the next fiscal year. For example, natural gas royalties have dropped recently due to lower market prices, and gaming revenues are expected to be lower as the use of video lottery terminals falls off.

At the same time, government expenses are expected to increase, especially in the largest segments of the budget: health, education, and social services. This is mainly due to negotiated salary and wage increments and higher costs for health-care services and community supports. Health-care expenses alone have increased by more than $600 million since 2003–2004.

The cost of funding government pension plans and other retiree benefits is also expected to jump considerably.

Nova Scotia remains committed to debt reduction and would like to continue the considerable progress made in recent years. However, while payments on the province's debt have reduced its growth, more aggressive measures will be needed to start reducing the debt in 2007–20008, according to the debt reduction plan.

Finally, the province is facing some new economic realities. The population is starting to decline, and people, on average, are getting older. These trends have implications for everything from the labour supply to federal transfer payments.

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It is clear that the budget planning process for 2007–2008 will be more challenging than it has been in recent years. Government must find ways to control and reduce spending, which may include delaying action on some priorities until they are affordable. At the same time, government must ensure that there are sufficient revenues to cover costs, invest in key development priorities, and promote debt reduction.

Fiscal Overview 2007 outlines the province's economic and fiscal situation, based on the numbers and statistics produced for the province's December 2006 budget forecast update.[1] It is intended to provide a fiscal context for planning, both inside and outside of government, for the 2007–2008 fiscal year and future years.

1 Numbers are based on the 2006–2007 Province of Nova Scotia Budget, and Forecast Update, as of December 19, 2006. Unless otherwise indicated, source numbers come from the Nova Scotia Department of Finance and Statistics Canada.

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Fiscal Summary

The Government of Nova Scotia has tabled five consecutive balanced budgets, and produced surpluses at the end of each of the last four years.

As of the December 2006, a surplus is projected for the end of fiscal 2006–2007, although it is $8.8 million lower than estimated in the budget.

Fiscal Summary

($ Millions)	2002–2003	2003–2004	2004–2005	2005–2006	2006–2007(f)*
Revenue					
Ordinary Revenue	4958.8	5355.9	5854.9	6262.2	6587.9
Expenses					
Net Program Expenses	4570.5	4797.2	5185.4	5566.3	6016.8
Net Debt Service Costs	847.2	856.1	890.4	863.4	830.9
Pension Valuation Adjustment	(149.6)	(12.4)	6.2	30.0	69.0
	5268.1	**5640.9**	**6082.0**	**6459.7**	**6916.7**
Net Impact of Consolidation and Accounting Changes	(2.7)	(19.0)	47.8	80.2	53.2
Net Income from GBEs	338.4	333.4	349.5	345.4	340.3
Unusual Item	1.4	8.7			
Provincial Surplus	**27.8**	**38.1**	**170.2**	**228.1**	**64.7**
Surplus Allocation					
Components of the Debt Reduction Plan					
Debt Retirement Contingency				4.0	4.0
Debt Retirement Fund			6.0		
Offshore Offset Agreement				57.1	57.4
Strategic Infrastructure Investment				85.0	
Other / Debt Reduction	27.8	38.1	164.2	82.0	3.3
	27.8	**38.1**	**170.2**	**228.1**	**64.7**

*(f) forecast

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Province of Nova Scotia—Economic Overview

Nova Scotia's economy has grown steadily over the last two decades, weathering some significant structural changes along the way. The province's real gross domestic product (GDP) has averaged 2.2 per cent, and the outlook to 2010 suggests the trend will continue.

Offshore natural gas has been a major stimulus of economic activity in the last few years and resulted in an increase in offshore revenues in 2005 and 2006. Nova Scotia has also seen record high employment levels and strong growth in consumer spending, retail trade, and investments in residential housing.

While the continued growth is positive, the pace of growth has generally been below the Canadian average. As well, recent results have not matched the growth from 1997 to 2002, when real GDP averaged 4 per cent.

Changing demographics are having a major effect on the economy. Nova Scotians born in the post-war years are now moving into retirement, while many younger Nova Scotians are choosing to pursue their careers outside of the province.

The slower population growth of recent years is now turning into a decline in Nova Scotia's population for the first time in recent memory. The province is also getting smaller in relative terms, as other Canadian provinces see their populations continue to grow.

A larger population of elderly Nova Scotians translates into increased demands on health care and other programs. Meanwhile, the province is starting to see fewer taxpayers in the active workforce to cover the added cost of these programs and services.

Employment levels reached a record high in 2005 with 443,100 workers employed in Nova Scotia, before dropping back slightly in 2006 to 441,800. The unemployment rate as of December 2006 stood at 7.9 per cent, down from 8.4 per cent one year earlier, in part due to the shrinking labour force as measured against declining employment.

Although employment levels are high, labour supply is becoming a serious problem for many industries and businesses. Nova Scotia employers must aggressively compete with counterparts in other provinces and countries to attract and keep skilled workers. Government must also provide comparable programs, services, and taxation levels for individuals to keep them in the province.

Nova Scotia's economy has been moving away from resource industries such as fishing, mining, and industry—its traditional base—to the services sector. More and more people are working in service industries like health care, retail, construction, information technology, and other scientific and technical jobs. In 2005 the production of goods accounted for 23.2 per cent of GDP, while services accounted for 76.8 per cent.

This change, while difficult for some, has brought a number of positives. Jobs in the information technology, finance, and insurance industries, for example, tend to pay relatively well. There are also signs that companies are becoming more productive, through higher capital investment and better use of technology.

Current Economic Indicators

	Percentage	
	Canada	Nova Scotia
Real GDP (2005)	2.9	1.6
Employment (2006/2005)	1.9	-0.3
Unemployment Rate (2006)	6.3	7.9
Consumer Price Index (YTD Nov 06/YTD Nov 05)	2.0	2.2
Retail Sales (YTD Oct 06/YTD Oct 05)	6.4	6.8
Labour Income (YTD Q3 06/YTD Q3 05)	6.1	4.0
Value of Building Permits (YTD Nov 06/YTD Nov 05)	10.7	4.9
Housing Starts–All Areas (YTD Q3 06/YTD Q3 05)	1.4	3.5
Manufacturing Shipments (YTD Nov 06/YTD Nov 05)	-0.5	-5.7
Inter. Merchand. Exports of Goods (YTD Nov 06/YTD Nov 05)	1.1	-11.3

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Nova Scotia's population has been slowly shifting from the rural to the urban areas, and more rural residents are commuting to work in the Halifax Regional Municipality, travelling an hour or more each way. This means a growing demand for infrastructure and services in smaller communities with relatively few taxpayers.

Global factors are increasingly at play in Nova Scotia's economy, and Nova Scotia businesses are more involved in international trade. In 2006, the province was affected by slowing economic growth in both Canada and the United States, along with the exchange rate and weak commodity prices.

Nova Scotia's international exports of merchandise goods dropped 11.5 per cent (January to November 2006).

This has been offset, however, by stronger domestic demand. The latest available 2006 figures show a number of positive trends:

- There was significant growth in retail trade, up 6.8 per cent compared to the Canadian average of 6.4 per cent (January to October).
- Investments in residential housing were 5 per cent higher, supported by a 4.7 per cent increase in renovation expenditures (January to September).

Inflation has been lower than expected with the 2006 Consumer Price Index forecast to drop to 2.3 per cent compared to the budget projection of 2.9 per cent.

Province of Nova Scotia Revenues

Current Trends

Nova Scotia is forecasting total revenues for 2006–2007 of $6.928 billion, with $4.557 billion from provincial sources and $2.371 billion from federal sources.[2]

Since 1996–1997, total annual revenues have grown by approximately $2.67 billion, averaging growth of 5.0 per cent per year.

Overall, Nova Scotia's own-source revenues have grown from 61.4 per cent of Nova Scotia's total revenues to 65.8 per cent, an increase of approximately $1.94 billion, or 5.8 per cent per year, since 1996–1997.

Provincial tax revenues are a significant source of funds for Nova Scotia. The main provincial sources are personal income taxes (PIT), corporate income taxes (CIT), and harmonized sales taxes (HST), amounting to 45.2 per cent of total revenues.

A strong economy has led to growth in income tax revenues, from 25 per cent of total revenues in 1996–1997 to 29.7 per cent in 2006–2007. Sales taxes have remained fairly constant at approximately 16 per cent of total revenues over this period, and this year will equate to $1.075 billion or 15.5 per cent of revenues.

Other key provincial revenues come from offshore royalties and motive fuel taxes, as well as from the net income generated by government business enterprises (GBEs) such as the Nova Scotia Liquor Corporation.

Although the total dollar value of motive fuel excise taxes has grown from $199 million in 1996–1997 to $248.9 million in 2006–2007, the relative importance of this revenue source has declined from 4.7 per cent of total revenues to 3.6 per cent over the same period.

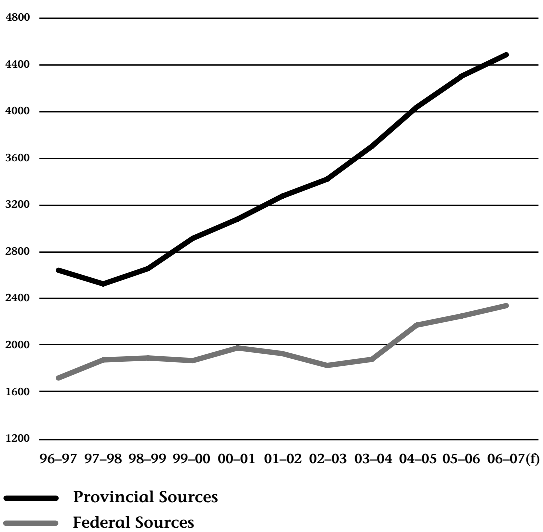
2 Numbers are calculated based on total consolidated fund revenues and net income from government business enterprises. Revenue projections reflect information available as of the December 19, 2006, budget forecast update.

Federal sources have grown on average by 3.96 per cent per year since 1996–1997. However, as a percentage of Nova Scotia's total revenues, they have declined from 38.6 per cent to 34.2 per cent in 2006–2007.

Revenues by Source

(Provincial = 65.8%; Federal = 34.2%)

($ millions)



The Government of Canada has acknowledged a fiscal imbalance in Canada, between the federal and provincial levels of government, and among provinces themselves. Small provinces like Nova Scotia do not have the capacity to fund expensive national programs like health care and education without assistance from the federal government that keeps pace with rising costs.

Federal payments for health care and social programs, provided to all provinces through the Canada Health Transfer (CHT) and the Canada Social Transfer (CST), are forecast to be $868.9 million in 2006–2007. At 12.5 per cent of Nova Scotia's total revenues, this represents about the same proportion of the budget as in 1996–1997. Meanwhile, our costs for Health and Community Services alone have gone up from 43.7 per cent to 51.7 per cent of the budget.

While Equalization payments have increased over the last decade, each year they become a smaller proportion of Nova Scotia's budget—decreasing from 26.2 per cent of total revenues in 1996–1997 to 20 per cent in 2006–2007, or $1.39 billion. Meanwhile, Nova Scotia's fiscal capacity has remained virtually unchanged over the last few years.

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There is considerable uncertainty about how much Nova Scotia will receive for Equalization in the coming years.

Since October 2004, the Government of Canada has used a two-part formula to allocate provincial Equalization entitlements from the fixed amount available. The calculation combined each province's average fiscal capacity and its Equalization entitlement over the last three years.

While the total available for Equalization in 2007–2008 has increased, a new formula was used to distribute the funds. The new base equalization amount for 2007–2008, provided to provinces on January 17, 2007, reflects average fiscal capacity, but does not factor in previous entitlements.

The result is that Nova Scotia's base Equalization number for 2007–2008, which will be used as a floor from which to calculate future entitlements, is $78 million lower than 2006–2007.

The timing of this change also means that Nova Scotia must plan its 2007–2008 budget using the lower Equalization number of $1.31 billion. The Government of Canada has promised that a more permanent solution to the fiscal imbalance problem will be announced as part of its spring budget. This may alter the allocations for 2007–2008.

In both the short and long terms, Nova Scotia will have considerable difficultly generating additional revenues from other sources to offset a drop—or inadequate growth—in federal revenues. Nova Scotia tax levels are already among the highest in Canada, so any increase in taxes would further compromise our competitive position with other provinces and jurisdictions.

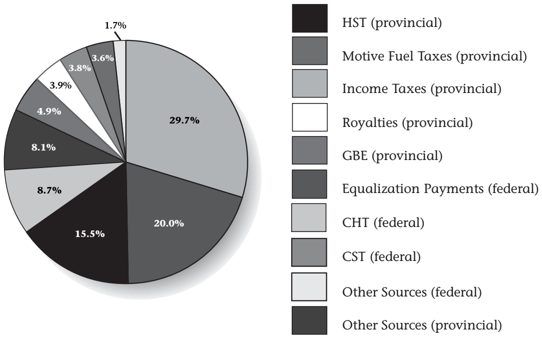
Nova Scotia's offshore industry has provided significant additional financial resources in recent years. There have been substantial increases in royalty revenues tied to gas production, and in some years companies have paid penalties for forfeiting offshore exploration licences.

However, offshore revenues are subject to change due to a number of factors, such as price of natural gas and the level of offshore exploration activity. They will also decline as gas production volumes fall through the life of the Sable offshore project.

Under the provincial/federal Offshore Offset Accord, Nova Scotia received $830 million from the federal government in July 2005 to fulfil the terms of legal resource sharing agreements signed in the 1980s. The funds were immediately applied to the provincial debt and continue to generate savings in debt-servicing costs.

For accounting purposes, the $830 million is recognized over the eight-year term of the agreement and is brought in as revenue in each year. However, there is no further cash value to the offset amount, and it cannot be used to fund programs or services. The offset amount goes directly to the bottom line surplus and to net direct debt, as required under the terms of the legislated debt reduction plan.

Current Revenues by Source
(2006–2007: $6.928 billion)



Revenue Challenges

Nova Scotia needs sufficient revenues to cover the growing cost of programs and services. Slower growth in revenues overall, or a major drop in any one category, would jeopardize the province's ability to cover costs and invest in its priorities.

In recent years government has seen revenues increase in a number of areas, most notably in categories related to the production of offshore natural gas. However, some of these upward trend lines are flattening out or even declining.

Revenues also naturally fluctuate widely each year due to cyclical economic conditions and changes in market factors. An example is the December 2006 forecast for petroleum royalties, which has been adjusted downward by $7.0 million due to lower market prices for natural gas.

Beyond these normal ups and downs, some underlying trends pose risks for revenues.

The small decline in Nova Scotia's population means the province will see reduced funding for a wide assortment of government programs that are funded through per-capita formulas. When 2006 national census data is factored into these formulas, revenues may go down.

This year, federal health and social transfers are forecast to be $10.5 million lower than budget, as Nova Scotia gets a smaller share of the total funding for social programs relative to other provinces. We are also seeing indications that Nova Scotia's share of the national taxation pools may go down.

In some years, economic growth in Canada and the United States has helped increase provincial revenues through income tax revenues and other indicators of economic activity. However, with growth expected to be lower than some past years, revenues are not likely to rise.

Nova Scotia has few options to generate additional revenues from income taxes. The majority of Nova Scotia tax filers do not have the income levels of their counterparts in other regions. Roughly two-thirds of Nova Scotia tax filers earn less than $30,000 a year, and the top 8 per cent of Nova Scotia taxpayers carry over 49 per cent of the personal income tax burden.

Business Tax Rates
as of Jan. 1, 2007

	Nova Scotia	New Brunswick	Ontario	Alberta	Federal
General Income Tax	16%	12%	14%	10.0%	21%
Small Business Income Tax	5%	1.5%	5.5%	3%	12%
Large Corporations Tax (Capital Tax)	0.25%	0.20%	0.285%	0%	0%
Corporate Capital Tax	4%	3%	0.57– 0.855%	0%	1.25%

Ontario offers a 2% credit for manufacturing and processing profits, reducing the effective rates for these activities to 12%.

The federal government also charges a corporate surtax with an effective rate of 1.12% on large corporations.

Nova Scotia's own policies adopted to promote the province's competitiveness also come at a cost to revenues. Tax measures in the 2006–2007 budget will be phased in over the next few years to bring Nova Scotia's taxation levels more in line with those in other provinces. These include

- the reduction and eventual elimination of the large corporations tax by 2012
- increasing the basic personal exemption
- reducing energy costs through Your Energy Rebate
- the Post-Secondary Graduate Tax Credit, an incentive for graduates employed in Nova Scotia
- child and healthy living tax credits
- various other measures

These tax measures are estimated to save taxpayers in the range of $480 million over the next four fiscal years. As investments in the province's economic future, they will also pay unspecified long-term dividends. However, in the short term, they mean a reduction in provincial revenues—and ultimately less for program spending.

The Province of Nova Scotia's budget will be affected in 2007 by unilateral changes made at the federal level to income taxes. The Government of Canada announced a plan in fall 2006 to allow splitting of pension income for tax purposes, a policy choice that will cause provincial tax revenues to drop across Canada next year. The spring 2007 federal budget is likely to provide details on this and other potential tax changes.

Revenues from Nova Scotia's offshore will depend on the volume of natural gas available for sale, along with world energy prices. In the absence of new development, offshore revenues will likely peak in 2007–2008 and begin to decline in 2008–2009. Revenues for royalties and offshore offset totalled $185 million in 2005–2006 and are forecast to be $330.4 million in 2006–2007.

The revised Deep Panuke project could provide renewed emphasis on the offshore. However, if offshore revenues are to be a sustainable source of revenue into the next decade, new offshore developments will be required to replace the Sable Offshore Energy Project reserves.

Finally, Nova Scotia has reduced some sources of revenue for social policy reasons. For example, revenues from gaming, which had been rising, will decrease over the next couple of years as the Nova Scotia Gaming Strategy is fully implemented.

Province of Nova Scotia Expenses

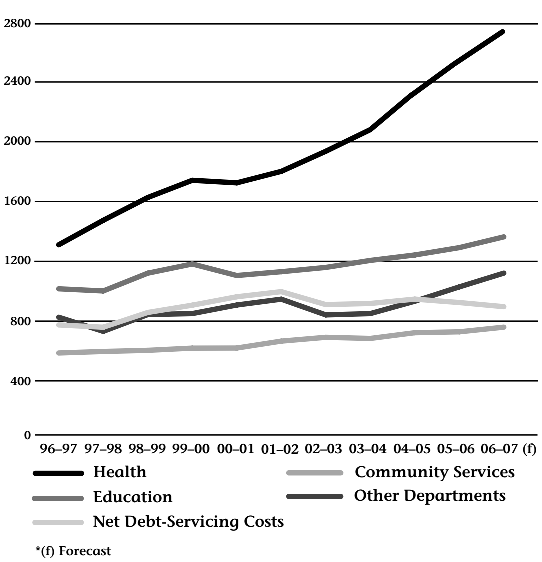
Current Trends

The majority of Nova Scotia's spending covers health and social services—primarily through the departments of Health, Education, and Community Services—along with debt-servicing costs.

The remaining government programs account for just 16 per cent of total spending. From that envelope, government allocates spending on provincial roads, economic development, the justice system, natural resources, the environment, and all other demands on the provincial government.

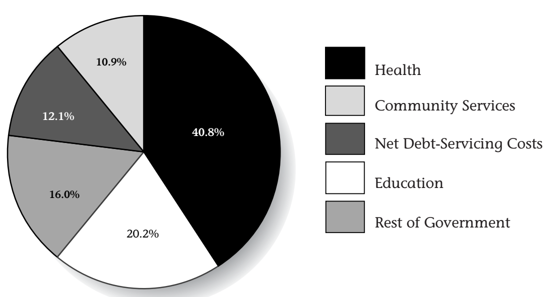
Spending Trends

($ millions)



Total Spending

(2006–2007: $6.848 billion)



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Health and Health-Care Spending

Health care has been the fastest-growing segment of the budget, averaging annual increases of 7.9 per cent since 1996–1997, almost 3 per cent higher than average revenue growth.

Health expenses have increased by more than $600 million since 2003–2004 alone[3] and have more than doubled in the last decade from $1.318 billion in 1996–1997.

For 2006–2007, health-care expenses are estimated at $2.793 billion. This is

- $220.7 million (8.6 per cent) higher than in 2005–2006
- almost 41 per cent of total government expenses
- 46.4 per cent of net program expenses

Of the total cost for health care, almost 47 per cent goes to running hospitals, including nursing and other staff. Just over 20 per cent goes to paying physicians.
The remaining 33 per cent is divided up among long-term care, Pharmacare, home care, emergency services, and other health services and initiatives.

The costs of all of these categories have been increasing steadily each year. From 1996 to 2006 costs have changed as follows:[4]

- The cost of running hospitals has gone up from $729 million to $1.290 billion (from 55 per cent of total health expenses down to 46.6 per cent).
- Payments to physicians increased from $268 million to $565 million, consistently just over 20 per cent of total expenses.
- The cost of long-term care has escalated from approximately $104 million to $326 million, rising from 7.9 per cent to 11.8 per cent of the total.

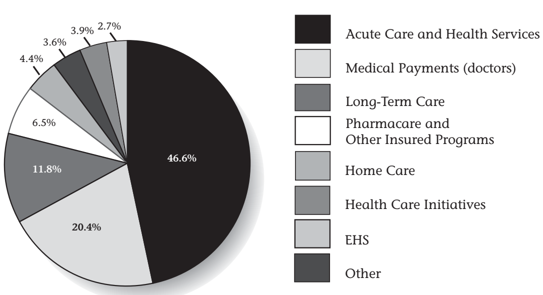
3 While prior period figures have been restated to reflect changes in accounting policy standards over the years, there could be minor differences in the composition of the balances.

4 Numbers compared against 2006–2007 budget.

- Pharmacare and other insured services have escalated from $55 million to $180 million, a proportional share increase from 4.2 per cent to 6.5 per cent.

- Spending for home care has stayed at just over 4 per cent, but the net dollar value has increased from $57 million to $121 million.

Health Spending
(as per 2006–2007 budget)



Education Spending

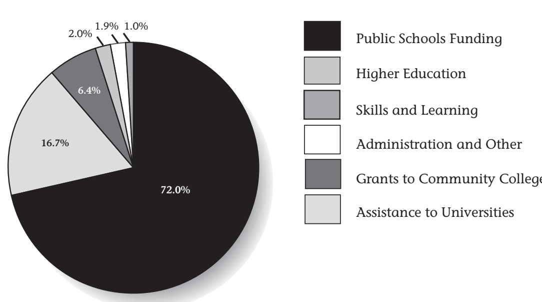
Education (including primary to grade 12 and colleges and universities) is Nova Scotia's second-largest annual program expense, accounting for 20 per cent of net expenses—or $1.380 billion annually (2006–2007).

While the dollar value of program spending on education has increased by some $400 million since 1996–1997, spending on education as a percentage of total provincial spending has declined from 22.8 per cent to 20.2 per cent.

Public school enrolment has gone down, from 163,941 in 1996–1997 to 148,514 in 2003–2004. It is projected to decline to 139,296 in 2006–2007 and 135,916 in 2007–2008.

Overall funding for education increased by 6.5 per cent or $85 million from 2005–2006 to 2006–2007.

Education Spending
(as per 2006–2007 budget)



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Debt-Servicing Costs

Nova Scotia's net direct debt (NDD) at March 31, 2006, was $12.239 billion. Net direct debt went down in 2005–2006 for the second year in a row, as government produced a surplus higher than its capital spending costs.[5]

Net debt-servicing costs are forecast to be $831 million for 2006–2007, about $45 million less than budget.

Debt-servicing costs have increased approximately $144 million since 1996–1997, largely due to the rise in the level of debt plus the inclusion for accounting purposes of interest on unfunded pension liabilities and other post-retirement benefits.

However, over the same time period, net debt-servicing costs as a percentage of total net spending have declined from 16.1 per cent to 12.1 per cent.

Net debt-servicing costs as a percentage of revenue have declined from 18.1 per cent in 2000–2001 to 13.1 per cent in 2005–2006 and are forecast to further decline to 12.0 per cent for 2006–2007.

As a result of good fiscal and debt management practices, the province's credit rating was upgraded by all three major bond-rating agencies in 2006. Such trends provide Nova Scotia with easier access to financial markets.

Government increased capital investment in infrastructure—highways, schools, and other buildings—in 2006–2007. As a result, even though balanced budgets continue, net direct debt is not scheduled to go down until 2007–2008.

Community Services

Funding for Community Services represents government's third-largest program expense, at $748 million for 2006–2007.

This has grown by $203 million, or 37 per cent, since 1996–1997, although the share of total spending on Community Services has declined from 12.8 per cent to 10.9 per cent over the same time period.

5 Surplus was greater than the change in net book value of tangible capital assets.

Spending Challenges

Expenses have been growing at almost the same pace as revenues in recent years, but if no changes are made they are at risk of outpacing revenues.

The December forecast for budget 2006–2007 anticipates higher costs in a number of areas. As a result, the Minister of Finance has asked departments to defer or eliminate non-essential spending for the rest of the fiscal year. The goal is to ensure that the province ends 2006–2007 with the required legislated surplus.

The government faces a number of challenges on the expense side in planning the 2007–2008 budget:

- Almost all government expenses are expected to continue an upward trend in 2007–2008
- Unanticipated new pressures from 2006–2007 are likely to carry over into the next fiscal year
- The full annual cost of new programs introduced in the July 2006 budget must be included in the 2007–2008 budget.
- Additional investments are required to build the province's economy and promote healthy individuals and communities.

Keeping up with health-care expenses alone will be a major challenge next year. Health expenses have been growing at a faster rate than revenues, and more quickly than ever before. And because of the size of the health budget, even small increases take away funding that could be used for other priority areas.

As well, it is extremely difficult to address or offset some of the underlying factors in the rise of health-care costs: the aging population, wage settlements, drug costs, and increased demand for more sophisticated and high-tech services.

If all trends remain the same, health-care expenses could continue to grow at approximately 8 per cent each year. With Nova Scotia's average revenue growth at 5 per cent, and federal source revenues growing at only 4 per cent, this trend is a great challenge for Nova Scotia, as it is for all provinces.

Choices for the 2007–2008 budget will also be affected by a number of other significant spending pressures.

Due to the size of government pension plans, any change in pension assumptions could represent a significant added cost to government both in the current fiscal year and in 2007–2008. Each year pension plan expenses are affected by a variety of factors, such as asset returns, retiree profiles, and anticipated pension expenses.

All government programs are facing normal increases in operating costs, related to higher wages, fuel prices, and changing technology. Wages and salaries for health-care providers, educators, and other public servants are the largest component of the province's total expenses across the public service. These account for approximately 63 per cent of all program spending; for every one per cent increase, government expenses go up by approximately $38 million.

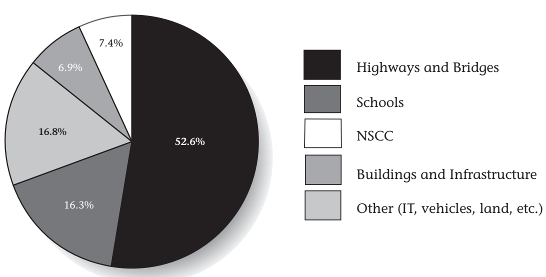
Nova Scotia's capacity to spend is constrained by its legislated requirements to balance the budget and reduce debt over time. As a result, spending plans for current and future years should be in line with revenues available or projected.

In addition to covering rising costs for existing programs, the government must find ways to invest more in the province's future. There is a need to promote economic development, ensure an educated workforce, improve our environment, and modernize our youth justice system.

Education and training investments are required to strengthen Nova Scotia's competitive capacity, and these are costly. Nova Scotia will need federal support to address priorities such as bringing university tuition closer to the Canadian average, and expanding skills training to meet changing workforce needs.

At the same time, children and youth who run into trouble with the law need access to social supports that will help them develop into happy, well-adjusted adults.

Tangible Capital Asset Spending
(as per 2006–2007 budget: $335 million)



Nova Scotia needs to address its outdated infrastructure with substantial ongoing investment. The infrastructure deficit is estimated at more than $3 billion for roads and highways alone. Although more than $300 million per year is currently spent on capital improvements—for roads and highways, schools, hospitals and other buildings, information technology assets and other equipment such as vehicles—this spending is not sufficient to address the province's infrastructure needs.

Nova Scotia also needs to build new infrastructure, so that the province will be positioned to take its place in the global economy. The province needs to seize promising opportunities like developing Nova Scotia as a transportation gateway.

It is apparent that government must find ways to control costs and reduce spending in the 2007–2008 budget. At the same time, government must invest in those priorities that pay social and economic dividends for the province in years to come.

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Province of Nova Scotia—Debt Management

Current Trends

The Province of Nova Scotia has taken a number of steps to stop the growth of Nova Scotia's debt in recent years, including legislation governing balanced budgets, surpluses, and debt reduction.

The government's adoption of a more disciplined fiscal management system has resulted in five consecutive balanced budgets, and the 2005–2006 surplus was the highest yet at $228.1 million.

Since 2001–2002, Nova Scotia's net direct debt as a percentage of gross domestic product (GDP) has declined from 46.8 per cent to 39 per cent as of March 31, 2006. A further decline to approximately 38 per cent is forecast for the year-end March 31, 2007.

The Offshore Offset Agreement brought $830 million from the Government of Canada in July 2005. These funds were immediately used to pay down the gross debt, and this will result in permanently lower debt-servicing costs in years to come.

Challenges

Nova Scotia has taken a number of significant steps in managing the debt in recent years, stopping its growth by 2007–2008 and even seeing the first drops in net direct debt in recent memory.

However, these efforts must be sustained over many years to see any significant reductions in the overall debt load and to further improve key debt indicators such as net direct debt as a ratio of GDP.

In basic terms, Nova Scotia would need to generate $250 million in surpluses annually for almost 50 years to retire our debt. There is a long way to go.

It is a positive trend that debt-servicing costs have dropped as a proportion of the total budget in the last few years. However, paying interest on the debt still costs the government in the range of $830 million a year—12 cents of every dollar available to spend. It would be preferable to be able to apply these funds to program costs, such as health, education, and social services.

NOVA SCOTIA

As well, given the need for investment in the province's infrastructure, it is unlikely that the government will be able to substantially reduce capital spending in future years.

Although the province has been successful at lowering debt-servicing costs through a variety of means, these costs are partly influenced by factors beyond the province's control, such as interest rates and the value of the Canadian dollar.

NOVA SCOTIA

Conclusion

The Province of Nova Scotia must carefully manage its resources in 2007–2008 to position Nova Scotia to take advantage of long-term opportunities, while addressing current year pressures and needs. Government must continue with a prudent approach to fiscal planning and ensure that the provincial budget responds to the changing fiscal environment.

It is clear that some tough choices will have to be made in the 2007–2008 budget:

- Revenues overall are not as strong as they have been, and many existing revenue categories are at risk of declining. There are no windfall revenues expected from any source.
- Federal revenues are subject to change. It is not yet known if a promised solution to the fiscal imbalance will address Nova Scotia's needs. Potential changes in programs like Equalization and federal taxation could cause serious problems for Nova Scotia.
- Expenses are rising overall. Government must contain growth, without compromising the quality of our health-care, education, infrastructure, and social support systems.
- The province must continue to invest in key priorities that will help the province grow and prosper.

Priorities must be carefully evaluated and set in these challenging conditions.