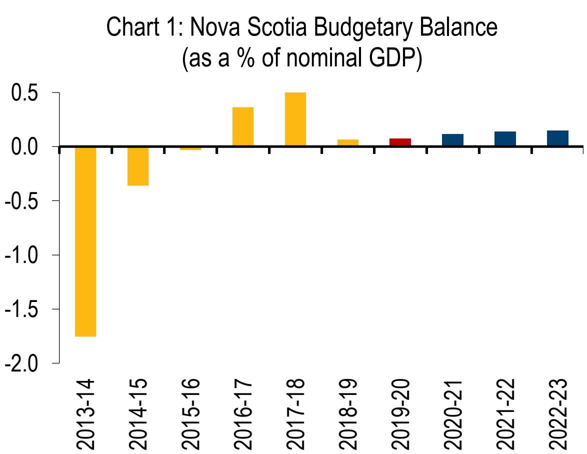
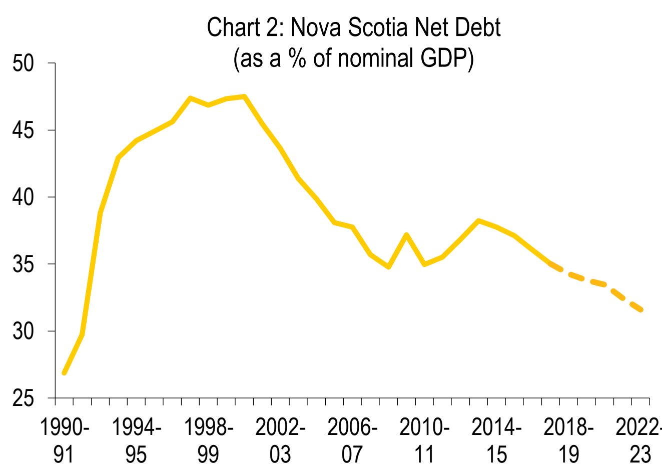
Laurentian Bank Securities
ECONOMIC RESEARCH AND STRATEGY

The 2019 Nova Scotia Budget: Focus on debt sustainability

Finance Minister Karen Casey released yesterday the Liberal government's fourth consecutive balanced budget, 5 years after taking power in late 2013. Budget 2019 forecasts a $33.6M (0.1% of GDP) surplus in FY 2019-20. The surplus is expected to almost double to $73.4M up to the end of the four year forecast in 2022-23, but to stay constant as a share of GDP (Chart 1). There are no new major tax increases or reductions in this budget. Underpinning this fiscal projection are moderate increases in total revenues (2.4% annual average growth) and total expenditures (2.3% annual average growth) from FY 2019-20 to 2022-23. Expenditure growth below the average annual nominal GDP growth forecast of 3.1% is indicative of governmental spending being under control. Overall, consistent surpluses allowed the province to reduce its net debt burden to its lowest level since 1992, a positive development noted by both investors and rating agencies (Chart 2).[1]



Source: Nova Scotia gvt., Stat. Can., LBS Econ. Res. and Strategy.



Source : Nova Scotia Government, Government of Canada Fiscal Reference Tables, LBS Econ. Res. and Strategy.

After running above trend in 2016 and 2017, real GDP growth slowed to 0.9% in 2018. Both due to slowing global economic momentum and domestic factors such as the completion of major investment projects (the Maritime Link and the Macdonald Bridge redecking), the economic outlook in the province is soft. Indeed, while record high net international migration has helped to stabilize the population aged 0-39, the projected decline in the 40-64 year old population combined to a rising 65+ year old population will continue to restrict labour supply. In contrast, labour market developments had been positive in recent years. For instance, the unemployment rate declined sharply and is averaging a record low of 6.7% so far in 2019. Exports diversification towards Asia and stronger productivity gains will still be key positive factors for the province. For 2019 and 2020, the NS Finance staff forecasts real GDP growth of 0.8% and 0.9%, respectively.

[1] S&P upgraded Nova Scotia from A+ to AA- in September 2018.

In this context, the Nova Scotia government proposes modest increases in program spending in FY 2019-20, with a focus on health care. The largest single announcement is a $157M proposal to extend investment in health care facilities and equipment (the QEII New Generation Project and the CBRM Health Care Redevelopment project). Overall, the FY 2019-20 surplus is based on 1.4% growth in both revenues and total expenditures.[2] The budgetary balance for FY 2019-20 is also supported by a $1.9B equalization transfer payment, representing 18% of total revenues; a proportion that has been broadly stable since FY 2016-17.

Lastly, the Nova Scotia government focuses on achieving fiscal sustainability, which by definition means that the public net debt does not grow continuously as a share of GDP in the long run. Even though aging demographics will weigh on the long run fiscal outlook, investors will see positively the projected rapid decline in the net debt-to-GDP ratio from 38.2% in FY 2013-14 to 31.6% in FY 2022-23 (chart 2).

Highlights of the borrowing program

- For FY 2019-20, total borrowing requirements are scheduled to reach $1.5B, up from a fully completed $1.3B program in FY 2018-19.
- More than half of the FY 2018-19 borrowing program was completed through two floating rate notes (FRN, $615M CDOR MTN FRN and $100M CORRA MTN FRN). For FY 2019-20, FRN will remain a flexible tool available to the issuer to meet part of its funding needs.
- There is also a possibility for the issuer to benefit from the flatter yield curve to re-open its existing 30-year domestic benchmark and/or building a new 10-year benchmark.
- The borrowing program is no longer focussing on extending the outstanding debt's average term-to-maturity, which stands at 13.2 years (up from 12.8 a year ago).
- While the government does not plan to withdraw money from its discretionary sinking fund in FY 2019-20, the large $911.4M available in this account *could* be used, if needed, for policy, liquidity and debt management purposes.

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[2] The expenditure forecast includes consolidation and accounting adjustments.