

Newfoundland and Labrador: 2021–22 Budget

INITIAL STEPS ON THE ROAD TO RECOVERY

- **Budget balance forecasts:** **-\$1.6 bn (-5.2% of nominal GDP) in 2020–21 (FY21), -\$826 mn (-2.3%) in FY22, -\$587 mn (-1.6%) in FY23; surplus targeted for FY27, one year later than in Greene Report (chart 1).**
- **Net debt:** expected to reach **52% of nominal GDP in FY21, then decline to 47% in FY22 (chart 2).**
- **Real GDP growth forecast:** **+5.6% in 2021, +2.6% next year—consistent with the provincial economy returning to pre-pandemic level this year.**
- **Borrowings:** **\$1.7 bn in FY22, following \$2.8 bn total in FY21.**
- **Budget highlights the depth of the fiscal challenges facing NL, presents better-than-expected near-term results, and serves as a first step on the path to longer-run fiscal sustainability.**

OUR TAKE

It was well-established before the release of this fiscal plan that Newfoundland and Labrador faced a challenging fiscal and economic outlook following COVID-19; Budget highlights some of those challenges. Rather than a return to balance in FY23 as planned before COVID-19, surplus will have to wait until FY27. In FY21, among the provinces, NL is estimated to have carried the largest net debt burden per capita and as a share of GDP, as well as run the second-largest deficit as a portion of output. Long-run economic growth prospects remain constrained by population aging.

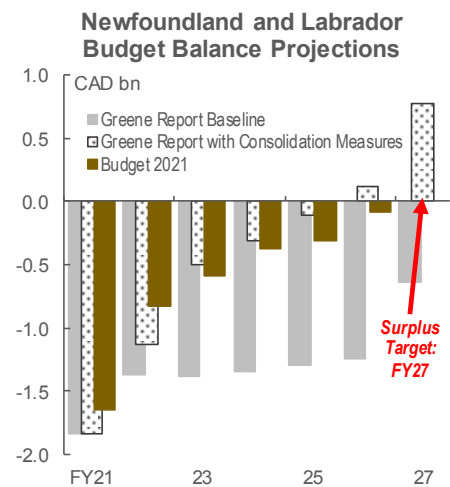
However, current-year and outer-year fiscal projections are stronger than anticipated and set in motion a plan to return to financial stability. As a share of GDP, the province anticipates that its net debt and deficit will decline significantly in FY22, with the latter expected to ease steadily and remain well below 2% of output through FY26. Projected interest costs as a share of revenue are elevated relative to those of other provinces, but remain well below the record highs experienced in the late 1990s and early 2000s. Alongside the commitment to balance by FY27, these figures should be positively received by the province's creditors. Charts 5–7 on page 3 compare key fiscal indicators in Newfoundland and Labrador to those of other Canadian jurisdictions.

A hefty projected economic rebound this year is partly behind the expected near-term improvement in NL's finances. The 5.6% real GDP gain penciled in for calendar year 2021 compares with a 3.8% private-sector average, and would be the strongest advance witnessed in the province since 2007, when crude output peaked. The forecast reflects expectations of a strong reopening effect as vaccine rollout continues, robust iron ore production, and the spillover impacts of strengthening crude and mineral prices. Accordingly, total revenues are forecast to rise by over 20% in FY22, with about one-third of the gain sourced from offshore royalties. That expansion is expected to come despite suspended activity at the Terra Nova oil field and West White Rose project in 2021.

CONTACTS

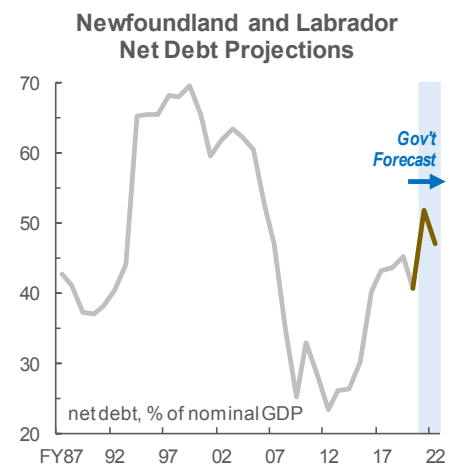
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Chart 1



Sources: Scotiabank Economics, NL Finance.

Chart 2



Sources: Scotiabank Economics, Finance Canada, NL Finance.

Federal transfers are set to increase by more than \$440 mn in FY22. The bulk of that increase relates to “Cost-Shared and Other Federal Revenues,” an umbrella category that includes all federal funding except for health and social transfers.

Helped by revenue gains, achieving the targets outlined in Budget requires less outer-year spending restraint than projected in the last multi-year pre-pandemic plan. Before COVID-19, the planned return to balance by FY23 relied on mean total expenditure annual declines of 2.5% in the last three years of the financial plan. The government is now targeting cuts of just 0.2% per year during FY24–26 (i.e., after the effects of pandemic-related spending unwind), which would result in roughly flat total expenditures between FY20 and FY26 (chart 3). That compares with forecasts of CPI gains in the 1.5–2% range and a flat or modestly falling population after this year.

The delayed and over-budget Muskrat Falls hydroelectricity project hangs over the financial projections. If the venture’s full costs are not recovered via the electricity rate base, it could result in a rise in taxpayer-supported provincial debt. On this front, we are encouraged by initial reports of constructive electricity rate mitigation discussions between the province and the Federal Government—though details have not been announced. The province will “begin a comprehensive analysis and reorganization” of Nalcor—the Crown corporation tasked with developing the venture—and conduct a review of the NL oil corporation. The Premier’s Economic Recovery Team Report—also called the Greene Report after its chair, Dame Moya Greene—suggested reviewing both entities as part of a plan to restore fiscal balance.

Other key elements of the Greene Report are included in the plan. NL personal income tax rates will be raised for all individuals earning more than \$135,973 per annum, with larger increases in higher brackets (table, p.3); the province will study potential sales tax rate increases that minimize impacts to low-income citizens. It also committed to implementing a “Future Fund” to pay down debt and support green energy development and technological innovation. Other new policy moves included: various public sector transformation and accountability initiatives, funds for COVID-19 personal protective equipment and vaccination, support for offshore oil projects, and broadband connectivity upgrades. The province also aims to settle 5,100 newcomers per year by 2026, and laid out funds for a range of integration initiatives.

Budget also announced nearly \$600 mn in FY22 infrastructure spending. The province estimates that these funds will generate 4.5k full-time equivalent positions. The largest single component of the allocation is the \$170 mn for highway maintenance; the plan also includes funds for healthcare facilities improvements, school construction, and marine infrastructure.

Oil price projections are typically prudent and in line with private-sector forecasts. Budget is based on a composite of price projections from 11 private-sector forecasts, which comes to a mean Brent value of 64 USD/bbl this fiscal year, and average of 62 USD/bbl over the ensuing four years (chart 4). In FY22, every additional 1 USD/bbl is associated with \$19 mn in offshore royalties. Budget also includes contingencies for oil price-related risks starting next fiscal year; the value of those provisions increases gradually from \$15 mn in FY23 to \$45 mn in FY26.

The government anticipates borrowings of \$1.7 bn this fiscal year. That follows an estimated \$2.8 bn total in FY21.

Fiscal Forecast Details

\$ millions except where noted

	FY21		FY22
	Bud.'20	Bud.'21	Bud.'21
Total Revenue	7,129	7,089	8,518
% change	1.0	0.5	20.2
Prov. Revenues	5,647	5,642	6,628
Fed. Transfers	1,482	1,447	1,890
Total Expenditure	8,967	8,733	9,344
% change	6.2	3.4	7.0
Programs	7,894	7,614	8,349
% change	6.7	2.9	9.7
Debt Costs	1,073	1,119	995
% of revenue	15.1	15.8	11.7
Budget Balance	-1,838	-1,644	-826
% of GDP	-6.2	-5.2	-2.3
Net Debt (bn)	16.4	16.3	17.2
% of GDP	55.5	51.7	47.1

Sources: Scotiabank Economics, Finance Canada, NL Finance.

Chart 3

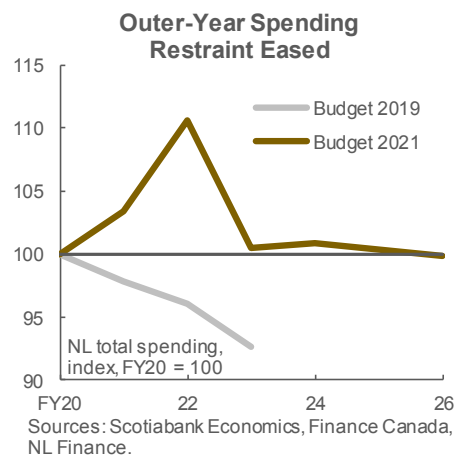


Chart 4

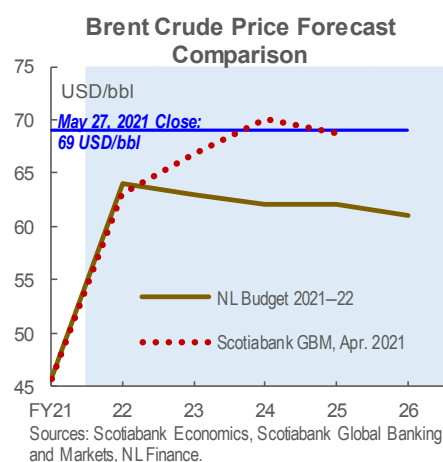
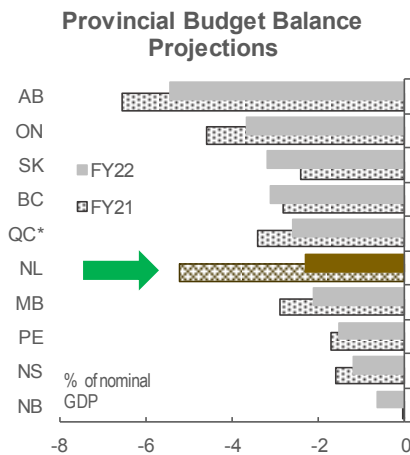
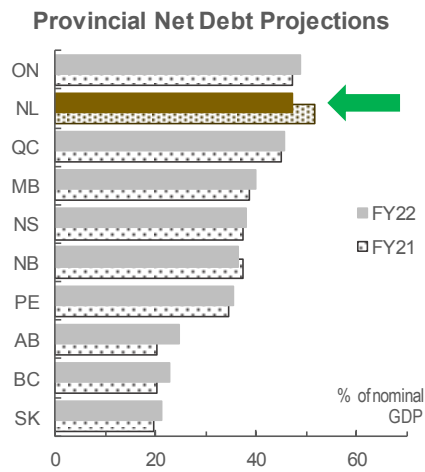


Chart 5



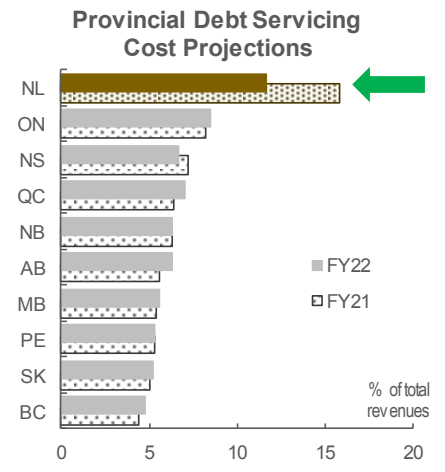
* Before Stabilization Reserve withdrawals.
Sources: Scotiabank Economics, Budget Documents.

Chart 6



Sources: Scotiabank Economics, Budget Documents.

Chart 7



Sources: Scotiabank Economics, Budget Documents.

Proposed PIT Rate Changes

Income Ranges in CAD

Income Range	Current	Budget 2021
< \$135,974	No Change	No Change
\$135,974–190,363	17.3%	17.8
\$190,964–250,000	18.3	19.8
\$250,001–500,000	18.3	20.8
\$500,001–1 mn	18.3	21.3
> \$1 mn	18.3	21.8

Sources: Scotiabank Economics, NL Finance.

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