Newfoundland and Labrador: 2018–19 Mid-Year Update

REVENUE BOOST NARROWS DEFICIT PROJECTION

SUMMARY

- **The Province of Newfoundland and Labrador's annual *Fall Fiscal and Economic* Update forecasts a smaller than previously anticipated budget deficit for fiscal 2018–19** (FY19). The $547.0 mn[1] shortfall compares favourably to the April 2018 budget (*Budget*) estimate of $682.9 mn. The government continues to forecast a return to black ink by FY23.
- **Expectations of higher revenues underlie the deficit revision.** The Province expects receipts to total $7.8 bn—$130 mn higher than forecast in *Budget*—while total revenues tracked previous projections. The government noted the rise in oil prices since April. Brent crude is now expected to average US$74/bbl in FY19; the prior estimate was US$63/bbl.
- **With a smaller budget deficit, borrowing requirements and net debt were lowered** (top table)**.** The Province expects to borrow just $1.25 bn to finance spending in FY19 versus $1.45 bn forecast in *Budget*. Net debt projections were reduced by $157 mn to $15.37 bn.
- **On the back of anticipated weakness in exports, the Province lowered its forecast real GDP decline for calendar year 2018 to 2.8%** (bottom table). Instead of the 2.8% real export rise projected in April, the government now expects a 1% decrease as a two-month labour stoppage resulted in reduced iron ore output (chart). Oil production, lifted in the first full year of operation at the Hebron offshore platform, will likely provide a partial offset but the government now foresees a 5.1% increase rather than the 6.4% gain forecast in April.
- **Forecasts for other sectors appear more conducive to revenue growth this year.** The Province foresees steady total employment this year—better than the 1% decline forecast in *Budget*—with household income also edged higher. It further cites a y/y decline in employment insurance beneficiaries to date this year as evidence of improving labour market conditions, though retail sales are expected to fall. A less precipitous contraction was forecast for business investment.
- **The government continues to emphasize its progress on longer-term cost control and economic diversification initiatives.** With respect to public sector modernization, it notes receipt of severance claims by 4,100 employees. The Province's investment in a St. John's contact centre, foray into deepwater oil production, targeted infrastructure outlays, and support for a major aquaculture venture highlighted its efforts to broaden its industrial base.

IMPLICATIONS

- **Newfoundland and Labrador's economic and fiscal position has largely evolved in line with our assessment of the balance of risks.** Absent more

[1] Figures reported in Canadian dollars unless otherwise stated.

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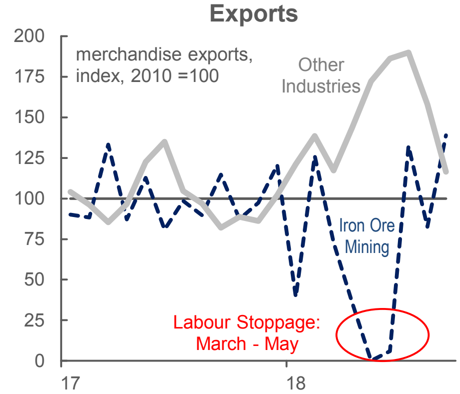
Fiscal Update
$ billions except where noted

	FY18	FY19	
	Final	Budget	Update
Total Revenue (mn)	7,280.1	7,673.4	7,803.6
Total Expenditure (mn)	8,190.9	8,356.3	8,350.6
Deficit (mn)	-910.8	-682.9	-547.0
% of GDP	*-2.8*	*-2.0*	*-1.6*
Net Debt	14.7	15.5	15.4
Borrowing Requirement	1.175	1.45	1.25

Sources: Newfoundland and Labrador Finance; nominal GDP forecast: Scotiabank Economics.

Newfoundland and Labrador Exports



Sources: Scotiabank Economics, Industry Canada.

Economic Assumptions
annual % change except where noted

	Calendar 2018	
	Budget	Update
Real GDP	-0.8	-2.8
Nominal GDP	1.3	3.6
Consumer Price Index	2.0	2.1
Population	-0.6	-0.6
Employment	-1.0	0.0
Participation Rate, %	57.8	59.0
Unemployment Rate, %	14.8	14.5
Employee Compensation	-1.1	-0.9
Household Income	0.7	0.9
Retail Sales	0.7	-0.9
Housing Starts	-10.1	0.1
Capital Investment	-9.3	-8.2

Source: Newfoundland and Labrador Finance.

detail, rising oil prices and an improving labour market—both of which we previously identified as offering upside potential for revenues—appear to have bolstered the government's coffers.

- **The return to balance remains challenging despite progress on deficit reduction.** Newfoundland and Labrador's current fiscal plan relies heavily on expenditure restraint. Assuming no change to prior revenue forecasts beyond FY19, total spending will still have to contract by an annual average of 1.4% to achieve the government's FY23 surplus target.
- **The Muskrat Falls hydroelectricity facility looms over the Province's outlook.** An inquiry into the project's significant cost overruns is proceeding in full public view and associated debt continues to be perceived by bond rating agencies as leaving the province's fiscal position vulnerable to adverse economic shocks. Waning construction activity on the project—which is still expected to finish next year—is also a key contributor to our forecast of falling private sector capital outlays this year, though the government now anticipates that other projects will propel a rebound in business investment approaching 7% in 2019.