



Dr. Sherry Cooper
Chief Economist, BMO Capital Markets

The Taxman Leaveth

Fiscal Year 09/10

Robert Kavcic
Economist

March 17, 2009
2:00 pm

The Province of New Brunswick is projecting a significant widening of its budget deficit to \$741 mln in FY2009/10 as it undertakes stimulus measures and tax cuts in a deteriorating economic environment. This marks the Province's largest budget deficit as a share of GDP (2.7%) since FY1987/88, but is accompanied by a plan to return to balance in four years and a long-awaited restructuring of the tax system. The deficit includes \$300 mln of pension-related expenses, resulting in a more modest \$441 mln shortfall if excluded. **The FY2008/09 budget deficit is now estimated at \$265 mln**, a modest improvement from December's \$285 mln estimate, but well below the \$19 mln surplus projected a year ago.

Total revenues will fall 0.6% to \$7.1 bln in FY2009/10, with own-source revenue falling 4.5%. An overhaul of the Province's tax system has been in progress for more than a year, and this budget provides the long-awaited four-year tax reduction plan. In total, there will be \$144 mln of tax cuts in FY2009/10, rising to \$380 mln by FY2012/13. The biggest element is a reduction in personal income taxes (\$118 mln this fiscal year, rising to \$323 mln by FY2012/13). This is accomplished by lowering all tax rates in 2009, and replacing the current four tax brackets/four tax rates structure with two brackets/two rates by 2012. By then, the two tax brackets will have

rates of 9% and 12% (the income level that jumps brackets will be \$37,893), down from a range of tax rates between 10.1% and 18% in 2008. Other tax savings on the personal side include a higher tuition rebate and enhanced benefits for low-income seniors.

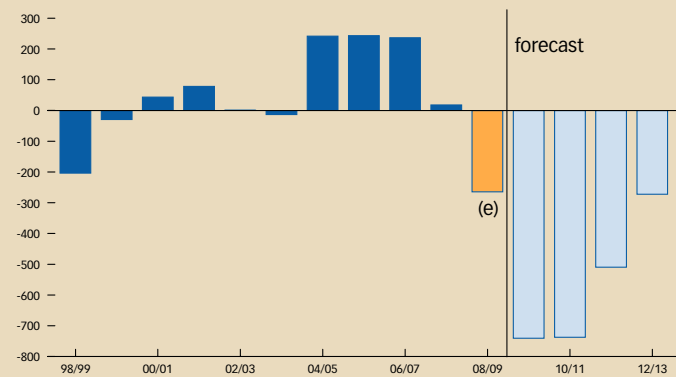
Corporate income taxes will also be cut, but the revenue impact will be relatively small, amounting to \$20 mln in FY2009/10 and \$44 mln by FY2012/13. The general corporate rate will be cut 1 ppt to 12% this year, and 1 ppt every year thereafter until it bottoms at 8% in 2012 (that would be the lowest in Canada at current rates).

Overall, the tax cuts are less than previously rumoured (about \$500 mln per year), but at the same time they will not be offset by increases in other taxes. A rise in the

Harmonized Sales Tax and a carbon tax were two ideas that were previously floated.

Total expenses are projected to rise 5.9% to \$7.8 bln in FY2009/10. This includes increases in education (1.6%) and health care (2.9%), but also a pointed attempt to reduce costs in the public sector through job cuts (700 this year) and wage freezes. Extraordinary pension expenses amount to \$300 mln this fiscal year, and are projected to remain at that level over the next four years.

Budgetary Balance
(\$ millions)



Source: Provincial forecasts e = estimate
*Forecasts include \$300 mln/yr in extraordinary pension expenses



Fiscal Outlook

(C\$ millions)

	actual		estimate	forecast
	06/07	07/08	08/09	09/10
Operating Revenues	6,649	6,919	7,138	7,097
Operating Expenditures	6,412	6,901	7,403	7,838
Budget Balance	237	18	(265)	(741)
<i>Year Ending March 31</i>				
Net Debt	6,578	6,976	7,304	8,273
% of GDP	26.1	26.2	26.1	30.1

Source: Provincial forecasts

Note: Totals may not add due to rounding.

The Province is also undertaking a \$1.2 bln capital investment program over the next two years (previously announced) to provide economic stimulus during the downturn. This includes \$379 mln for transportation infrastructure in FY2009/10 (a 16% increase over last year), \$160 mln over two years for education (upgrades and renovation) and \$67 mln for health care in FY2009/10. Municipal infrastructure, tourism and the environment will also be targeted in this broad investment program.

Net debt will increase \$969 mln to \$8.3 billion in the coming fiscal year as the Province finances the deficit and its infrastructure program. **The net debt-to-GDP ratio will rise 4 percentage**

points to 30.1% in FY2009/10. Total provincial borrowing requirements are pegged at \$1.6 bln this coming fiscal year.

The budget estimates are based on the assumption that the New Brunswick real GDP will contract 0.3% in 2009, which is more optimistic than our call of a 1.2% decline. **The New Brunswick economy is under pressure** as weak U.S. demand continues to hurt the export and manufacturing sectors, while domestic activity is also slowing. Major capital projects have fuelled construction activity, but those supports should fade as projects reach completion.

The information, opinions, estimates, projections and other materials contained herein are provided as of the date hereof and are subject to change without notice. Some of the information, opinions, estimates, projections and other materials contained herein have been obtained from numerous sources and Bank of Montreal ("BMO") and its affiliates make every effort to ensure that the contents thereof have been compiled or derived from sources believed to be reliable and to contain information and opinions which are accurate and complete. However, neither BMO nor its affiliates have independently verified or make any representation or warranty, express or implied, in respect thereof, take no responsibility for any errors and omissions which may be contained herein or accept any liability whatsoever for any loss arising from any use of or reliance on the information, opinions, estimates, projections and other materials contained herein whether relied upon by the recipient or user or any other third party (including, without limitation, any customer of the recipient or user). Information may be available to BMO and/or its affiliates that is not reflected herein. The information, opinions, estimates, projections and other materials contained herein are not to be construed as an offer to sell, a solicitation for or an offer to buy, any products or services referenced herein (including, without limitation, any commodities, securities or other financial instruments), nor shall such information, opinions, estimates, projections and other materials be considered as investment advice or as a recommendation to enter into any transaction. Additional information is available by contacting BMO or its relevant affiliate directly. BMO and/or its affiliates may make a market or deal as principal in the products (including, without limitation, any commodities, securities or other financial instruments) referenced herein. BMO, its affiliates, and/or their respective shareholders, directors, officers and/or employees may from time to time have long or short positions in any such products (including, without limitation, commodities, securities or other financial instruments). BMO Nesbitt Burns Inc. and/or BMO Capital Markets Corp., subsidiaries of BMO, may act as financial advisor and/or underwriter for certain of the corporations mentioned herein and may receive remuneration for same. "BMO Capital Markets" is a trade name used by the Bank of Montreal Investment Banking Group, which includes the wholesale/institutional arms of Bank of Montreal, BMO Nesbitt Burns Inc., BMO Nesbitt Burns Ltée/Ltd., BMO Capital Markets Corp. and Harris N.A., and BMO Capital Markets Limited. TO U.S. RESIDENTS: BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd., affiliates of BMO NB, furnish this report to U.S. residents and accept responsibility for the contents herein, except to the extent that it refers to securities of Bank of Montreal. Any U.S. person wishing to effect transactions in any security discussed herein should do so through BMO Capital Markets Corp. and/or BMO Nesbitt Burns Securities Ltd. TO U.K. RESIDENTS: The contents hereof are not directed at investors located in the U.K., other than persons described in Part VI of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.

™ - "BMO (M-bar roundel symbol) Capital Markets" is a trade-mark of Bank of Montreal, used under licence. © Copyright Bank of Montreal.