

Budget Highlights

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Got Oil?

Fiscal Year 10/11

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The Province of Newfoundland and Labrador is forecasting a reduced \$194.3 mln deficit (0.8% of GDP) for FY2010/11, as rebounding offshore oil revenues offset still-strong spending growth. The deficit is an improvement from the \$294.9 mln shortfall now estimated for FY2009/10, which marks another major oil-fuelled improvement (\$148 mln) from December's update. Recall that last year's budget projected a \$750 mln shortfall, but oil royalties have since been revised up by \$573 mln. Going forward, the Province expects to post deficits averaging \$175 mln in each of the next two fiscal years, as revenues and program spending both post sturdy increases.

Revenue is expected to rise 3.0% to \$6.6 bln in FY2010/11, reflecting a \$277 mln (14.7%) increase in oil royalties resulting from higher prices. The Province is assuming that oil will average US\$83.5/bbl in the coming fiscal year, up from last fiscal year's average of just

over \$70. At \$2.2 bln, offshore oil royalties will make up almost 33% of total revenue, about in-line with the average of the past three years. As usual, the volatility of oil prices is the biggest risk to the Province's financial projections. After cutting personal income tax rates in prior years (falling again in July 2010 on the second and third income brackets), there are a few new tax measures in this budget totalling a modest \$48.5 mln. This includes increases in the age amount non-refundable credit (from \$3,681 to \$5,000) and Low Income Senior's Benefit, and a 1 ppt reduction in the small business rate to 4%. The Province continues to aim for the lowest personal income tax rates in Atlantic Canada. Meantime, Federal transfers will total \$1.4 bln, up 7.8% from the prior year.

Fiscal Outlook

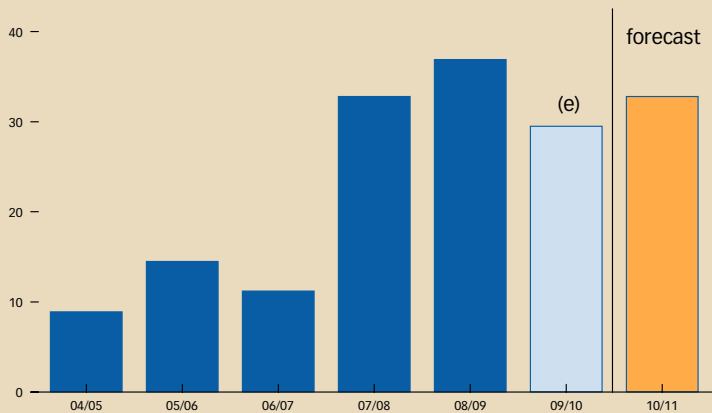
(C\$ millions)

	estimate		—forecast—	
	09/10	10/11	11/12	12/13
Revenues	6,393	6,585	6,737	6,691
Expenditures	6,873	6,986	7,191	7,173
Program Spending	5,970	6,177	6,364	6,312
Debt Service	903	809	827	861
Net Income of Gov't Business Enterprises	185	207	298	290
Consolidated Budget Balance	(294.9)	(194.3)	(156.9)	(192.1)

Source: Provincial forecasts () = deficit Note: Totals may not add due to rounding.

Offshore Royalties

(% of total revenue)



Source: Provincial forecasts e = estimate

Program spending is projected to grow a sturdy 3.5% to \$6.2 bln in FY2010/11, though that's down from the aggressive 8% pace seen during the past five fiscal years. Health care (7.4%) will continue to see strong growth, while education (1.8%) will see a more modest increase. Going forward, the Province is forecasting 1.9% annual program spending growth through FY2012/13, which will mark a 0.9%-per year contraction on a real per-capita basis (though all of the restraint takes place in the last year of the forecast horizon). The



commitment to spending this coming fiscal year echoes what most other Provinces have outlined this budget season, and the relatively small deficit gives them enough leeway to do that—assuming oil prices stay near current levels.

Infrastructure investment will remain robust in the Province, totalling about \$1 bln in FY2010/11, up from \$800 mln in the prior year (and pegged at more than \$5 bln over the next several years). At more than 3% of GDP, Newfoundland & Labrador’s infrastructure program remains among the most aggressive in Canada.

Net debt is expected to rise \$699 mln to \$9.2 bln by the end of FY2010/11, largely reflecting funding needs for infrastructure investments. Net debt now clocks in at 36% of GDP, about in-line with the Atlantic-Canada norm. Debt service costs will total 12.3% of revenue this coming fiscal year, falling from 14.1% thanks to lower pension-related expenses.

Newfoundland & Labrador’s economy suffered during the recession, amid a decline in oil prices and subsequent falloff in output. However, aggressive stimulus measures and rebounding commodity prices should drive a recovery this year—offshore oil output will continue to trail off, but the mining sector should bounce back after a strike-plagued 2009. All told, real GDP should rise a solid 3.7% this year and 2.9% in 2011—the Province is calling for slightly more aggressive growth of 4.0% and 3.1%.

The Bottom Line: Made possible by rebounding oil prices, the Province of Newfoundland & Labrador is opting to maintain firm spending growth and infrastructure investment in the coming fiscal year. However, with offshore royalties weighing in at a third of total revenue, oil prices remain an ever-present risk.

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