Nova Scotia: 2020–21 Fiscal Update

SIGNIFICANT PRESSURES FROM COVID-19, BUT WORST AVOIDED

SUMMARY

- **As seen across the world, Nova Scotia expects the COVID-19 pandemic to result in hefty deficit of $852.9 mn (2% of nominal GDP) in fiscal year 2020–21 (FY21), upending prior plans of surpluses through FY24.**
- **With a record economic contraction built into the current fiscal year, the government foresees a considerably larger-than-previously outlined net debt burden equal to 38.7% of provincial output in FY21.**
- **Risks remains and the pandemic's impacts will likely be felt for years to come, but Nova Scotia's relatively light caseload, diversified economy, and prudent pre-virus planning provide a basis for a solid recovery.**
- **We expect this update to be well-received by markets: new spending is constrained to COVID-19-related shocks, while also prioritizing capital investments that should strengthen growth.**

OUR TAKE

As in other provinces, this update reveals a more challenging fiscal and economic environment than before COVID-19. Rather than secure surpluses for the foreseeable future, Nova Scotia will now carry a large—albeit not historic—deficit and debt load forward. Given the prospect of a prolonged recovery and uncertain medium-term economic conditions, it, too, may have to balance long-run fiscal sustainability and support for at-risk sectors and occupations.

Still, Nova Scotia maintains a number of advantages over other jurisdictions. Its comparatively modest COVID-19 infection rates have enabled earlier easing of lockdown measures and participation in the travel bubble with neighbouring provinces, which should support its key tourism sector. Its status as a regional hub for high-value services and niche manufacturing strength should cushion it relative to less diversified local economies. Moreover, its healthy fiscal position before the pandemic appears as though it will prevent deeper red ink and heavier debt loads. Finally, funds from the Safe Restart Agreement with the federal government—not included in the plan—present upside for future balances.

Risks remain—notably around secondary waves, population, trade with China, and the virus' course in the US—but Nova Scotia appears in position to avoid the worst of the pandemic and benefit from the eventual recovery.

ECONOMIC OUTLOOK

As most elsewhere in the world, Nova Scotia expects the COVID-19 pandemic to result in a severe economic contraction—in both real and nominal terms—in 2020. Province-wide lockdowns and a worldwide drop in economic activity are forecast to result a 6% plunge in real output this year—far worse than the post-1982 record drop of just 1.2% witnessed during the Canada-

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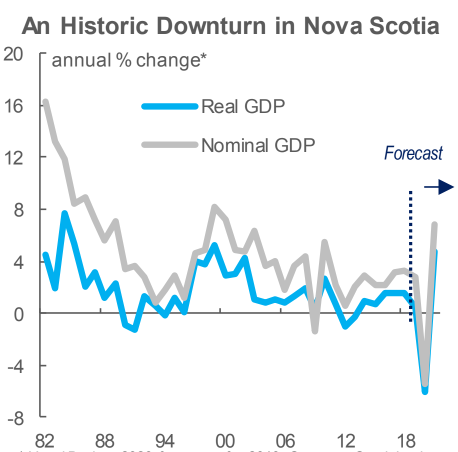
Table 1

Updated Fiscal Forecast
$ millions except where noted

	FY21 Budget	FY21 Update
Personal Income Tax (PIT)	2,980	2,930
Corporate Income Tax (CIT)	542	381
Harmonized Sales Tax (HST)	2,004	1,770
Other Taxes	666	614
Tax Revenues	6,191	5,694
Other Own-Source Revenue	496	472
Own-Source Revenue	**6,687**	**6,166**
Gov.Bus.Enterprises - Net Income	392	314
Ordinary Recoveries	667	665
Federal Transfers	3,851	3,920
Total Revenue	**11,597**	**11,065**
Program Spending	10,858	11,350
Debt Service	758	736
Total Expenditure	**11,616**	**12,086**
Consolidation & Adjustments	74	168
Provincial Balance	**55**	**-853**
Memo Items, %		
Budget Balance / GDP	0.1	-2.0
Debt Service / Revenue	6.5	6.7
Net Debt / GDP	33.3	38.7

Sources: Nova Scotia Finance; Statistics Canada.

Chart 1



* Used Budget 2020 forecasts for 2019. Sources: Scotiabank Economics, Statistics Canada, Nova Scotia Finance.

wide early 1990s recession (chart 1, p.1). As in New Brunswick, Quebec, and Manitoba, Nova Scotia anticipates a less pronounced contraction in nominal GDP than it does for real GDP. Presumably, this reflects expectations that imported inflation will dominate output gap effects. Even after a strong rebound next year, the Province expects nominal GDP to sit 4.3% below levels anticipated in *Budget 2020*.

Diversified trading relationships—a strength for Nova Scotia—unfortunately will not cushion against the impacts of a global economic downturn. Nominal export values to the US, China, and Europe are all down by more than 15% to date in 2020. This exacerbates the weakness in external shipments of staple pulp products and tires anticipated irrespective of the pandemic. Going forward, necessary adjustments to new health and safety practices are expected to challenge export-oriented firms.

Population growth, an important driver of Nova Scotia's recent expansion, is forecast to slow considerably versus its pre-virus trajectory. Immigration, interprovincial migration, and net non-permanent resident attraction all contributed to the 1.2% headcount expansion in Nova Scotia last year—the steepest climb since the 1970s (chart 2). Going forward, travel restrictions will likely weigh on all these flows, limiting population gains to an annual average of just 0.4% in the next two years, in contrast to the mean nearer 1% anticipated at budget time.

FISCAL DETAILS

Weaker revenues are a natural consequence of the more downcast economic outlook. Total government receipts are expected to come in more than $500 mn lower than anticipated as of just five months ago. Versus the *Budget 2020* projection for FY20, the 3% drop that would represent the sharpest annual revenue decline since at least FY87. Some $234 mn of the downward revision is attributable to softer harmonized sales tax revenues, with a further $161 mn from the projected plunge in corporate tax receipts. These changes reflect broad-based expectations of hard-hit consumption and investment.

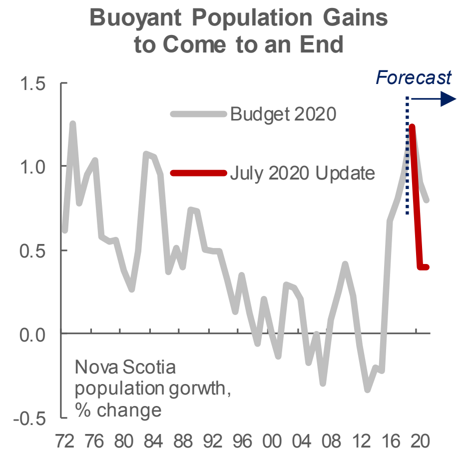
On the expenditure side of the ledger, the Department of Health and Wellness is forecast to contribute to almost 80% of the $492 mn cost overshoot relative to *Budget*, again reflecting the nature of this downturn. The implied 5.3% annual increase in total expenditures is, historically speaking, modest—spending growth exceeded that rate in every year from FY05–08, in FY12, and in FY18.

At $1.29 bn, projected FY21 capital spending is almost $250 mn higher than budgeted in February (chart 3)**.** The boost—to an already hefty bump announced in the last fiscal blueprint—is expected to support the provincial economy's near-term recovery and enhance its long-run productive capacity.

As a result of spending increases and the softer revenue outlook, the Province has penciled in a budget deficit of $852.9 mn (2% of nominal GDP) for the current fiscal year. That ends a run of four consecutive annual surpluses. It would be the largest nominal shortfall since at least FY87, but fall short of the GDP share over 3% set in FY2000, which followed a period of soft economic growth and major accounting changes. The 2% output share is also among the smallest reported by any province post-pandemic.

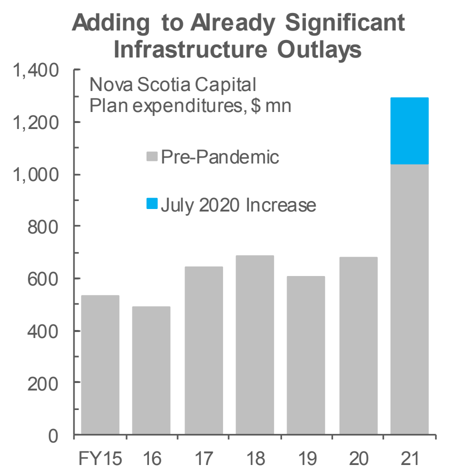
For provincial debt, the story is similar to that of the budget balance: higher, but for now, not historically so. At 38.7%, net debt's projected share of GDP falls well short of loads near 50% seen in the late 1990s and early 2000s (chart 4).

Chart 2



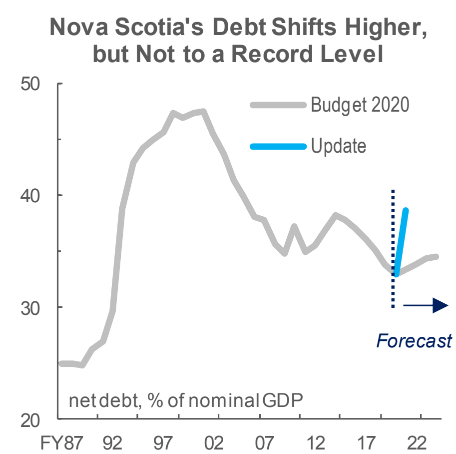
Sources: Scotiabank Economics, Statistics Canada, Nova Scotia Finance.

Chart 3



Sources: Scotiabank Economics, Nova Scotia Finance.

Chart 4



Sources: Scotiabank Economics, Finance Canada, Nova Scotia Finance.