BUDGET ANALYSIS

Nova Scotia: Budget 2023

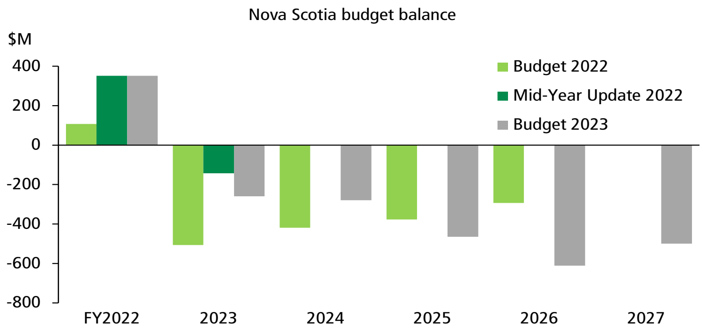
Surging Revenues to be Spent on Health Care and Capital Investments

By Marc Desormeaux, Principal Economist, and Randall Bartlett, Senior Director of Canadian Economics

HIGHLIGHTS

- Nova Scotia's 2023 budget continued to pencil in deficits for every year of the forecast starting in fiscal year 2022–23 (FY2023), following a short-lived surplus in FY2022 (graph 1). While revised lower in FY2023 and FY2024, deficits are now projected to be larger in the outer years of the forecast than in Budget 2022.
- In line with smaller fiscal shortfalls in the near term, the province expects to borrow $2.0B in FY2024, down $63M from the plan in Budget 2022. However, Nova Scotia now anticipates borrowing $2.3B and $2.2B in FY2025 and FY2026, respectively, up $720M and $955M versus last year's budget plan.
- Economic forecasts for calendar year 2023 were revised lower in respect of a softer global backdrop, but base case projections do not assume a recession. Outer-year economic forecasts have been revised higher, however, due to population growth and investment.

GRAPH 1
New Spending Drives Larger Deficit Projections



Sources: Nova Scotia Ministry of Finance and Desjardins Economic Studies

- The FY2023 revenue windfall lifted the trajectory of government revenues in the later years of the fiscal plan. That enabled much of the $3.4B in new spending in FY2024 and FY2025 combined versus last year's fiscal plan.
- Nova Scotia once again raised its population growth forecasts in light of the ongoing surge. To meet the needs of a growing population, it continues to plan significant increases in infrastructure spending that will raise its debt profile over time.
- Some investors and rating agencies will no doubt continue to worry about the province's rising debt burden. But we think the focus on long-run growth and public service provision is wise given Nova Scotia's particular economic situation and the sheer strength of recent population gains. The challenge will be to ensure that it hits its fiscal and infrastructure targets in a highly uncertain environment.

Our Takeaways

Today's budget maintains prior fiscal plans. Having devoted some of its revenue windfall towards new spending, there is little change to Nova Scotia's estimated timeline to balance.

While Nova Scotia's embrace of an upward-trending debt-to-GDP path since the pandemic has naturally worried some investors and rating agencies, we see compelling arguments for the strategy. Its recent surge in population growth is far more outside historical norms than pandemic-era gains witnessed in any other province. Given rising immigration targets, the draw of its diversified economy and status as Atlantic Canada's high-wage services hub, near-record headcount advances—and pressure on public services—could well persist. Meanwhile, damage caused last year by Hurricane Fiona lays bare the benefits of climate disruption-ready infrastructure. And of course, an aging population means there will be sustained pressure to spending on health care services and facilities.

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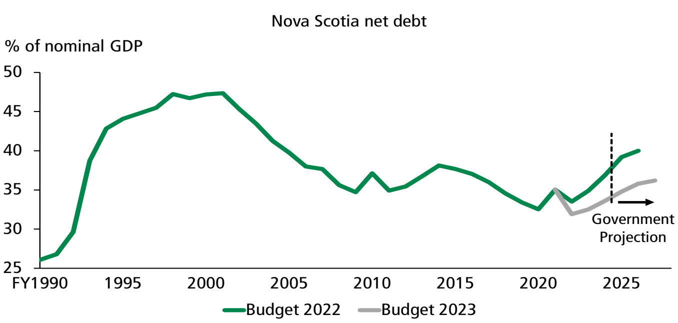
The challenge will be delivering on the targets laid out in the fiscal plan in an uncertain economic and financial environment. Nova Scotia would not be immune to the impacts of a global slowdown should one materialize, and we've seen the effects of input and labour product shortages on the capital plan this year. These factors will no doubt occupy Nova Scotia policymakers and investors alike in the coming years.

Medium-Term Deficits, Rising Debt Burden Maintained

Nova Scotia still anticipates red ink through FY2027. The province now projects shortfalls of $260M (-0.5% of nominal GDP) in FY2023, $279M (-0.5%) in FY2024, and $464M (-0.8%) in FY2025, a cumulative three-year reduction in the deficit of $300M. Its net debt is still expected to rise steadily, this time from about 32.5% of provincial output in FY2023 to 35.8% by FY2026. However, thanks to elevated levels of nominal GDP, that path is more than 4 percentage points lower than expected in last year's budget (graph 2). But if realized, the terminal level of the debt-to-GDP ratio would be among the highest of any province.

GRAPH 2
Debt Burden Shifts Lower, Still on Upward Track



Sources: Nova Scotia Ministry of Finance, Finance Canada, and Desjardins Economic Studies

In line with smaller fiscal shortfalls in the near term, the province expects to borrow $2.0B in FY2024, down $63M from the plan in Budget 2022. This followed borrowing of $1.35B in FY2023, which was near $300M below plan. However, Nova Scotia now anticipates borrowing $2.3B and $2.2B in FY2025 and FY2026, respectively, up $720M and $955M versus last year's budget plan. As a consequence, from FY2023 through FY2025, Nova Scotia is expected to borrow over $360M more than projected in Budget 2022 (table 1).

The government continues to note the influence of stepped-up infrastructure outlays—underway to support the needs of a growing population—in the planned borrowing trajectory. Last week, Nova Scotia released its FY2024 Capital Plan, which penciled in a record $1.62B in spending in FY2024. More than half of that sum is related to transportation infrastructure and health and education facilities. It comes after labour and input product shortages drove significant project delays and downward revisions to last year's Capital Plan (graph 3). Planned borrowing requirements for tangible capital assets have increased considerably in the outer years of the projection, rising by $96M in FY2024 relative to the Budget 2022 plan to nearly $1.1B. FY2025 and FY2026 are now expected to see borrowing requirements for tangible assets lifted by nearly $425M in each year.

TABLE 1
Updated Nova Scotia Projections

$ MILLIONS (UNLESS INDICATED)	2022–23	2023–24	2024–25	2025–26	2026–27
Borrowing Requirements					
Budget 2022	1,645.9	2,092.9	1,577.0	1,253.8	—
Budget 2023	**1,353.9**	**2,029.6**	**2,296.2**	**2,209.1**	**1,145.2**
Cash Operating Requirements					
Budget 2022	1,177.0	1,225.2	700.7	399.2	—
Budget 2023	**-8.9**	**1,839.1**	**1,416.9**	**1,252.1**	**1,003.0**
Real GDP Growth (%)*					
Budget 2022	2.1	1.6	-0.2	0.9	—
Budget 2023	**2.9**	**0.6**	**1.1**	**0.9**	**1.1**
Nominal GDP Growth (%)*					
Budget 2022	5.1	3.5	1.8	2.9	—
Budget 2023	**7.7**	**4.0**	**3.4**	**3.2**	**3.4**

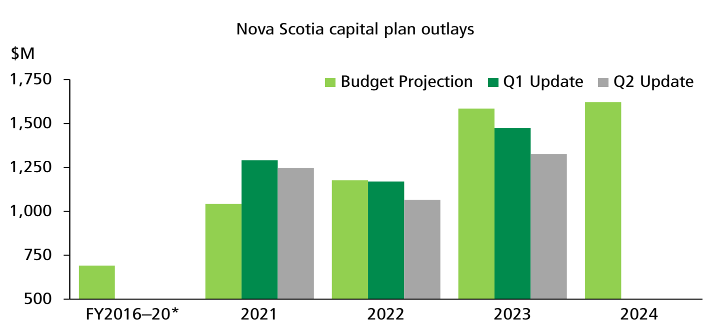
* FY2024 corresponds to calendar year 2023 and so on.
Sources: Nova Scotia Ministry of Finance and Desjardins Economic Studies

Revenues Stronger Despite Softer Economic Outlook

Like other provinces, Nova Scotia lowered its projections for economic growth in calendar year 2023. The fiscal plan is now based on real GDP growth of 0.6% this year, in respect of the drag from higher interest rates, weakening investment, and a softer global economic backdrop.

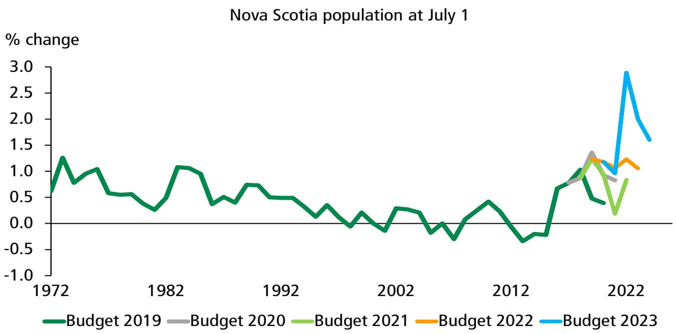
Still, revenues are expected to come in a combined $3.4B higher than forecast last year for FY2024 through FY2026. This is in large part the result of this fiscal year's starting point improvement of $1.7B.

GRAPH 3
Labour, Input Product Shortages Brought Capital Plan Delays



* Average for five fiscal years
Sources: Nova Scotia Ministry of Finance and Desjardins Economic Studies

GRAPH 4
Historically High Population Growth Argues For Higher Spending



Sources: Nova Scotia Ministry of Finance, Finance Canada, and Desjardins Economic Studies

Very strong population growth is expected to persist. Benefiting from record levels of international immigration and in-migration from other parts of Canada, Nova Scotia last year witnessed a headcount expansion rate nearly two and a half times its prior record (graph 4). That cushioned the province's economy and housing market against the effects of the pandemic and supported a surge in tax revenues. Interprovincial migration is expected to ease from unsustainably high rates of growth recently, driving some of the population growth slowdown, but not enough to keep the province from near-record headcount gains.

Spending Growth Boosted, Still Modest

With the benefit of additional revenues, the province will raise its spending profile for the next three fiscal years. Total expenditures for FY2024 and FY2025 exceed the targets in last year's budget by $1.5B and $1.3B, respectively, partly offsetting the increase in government receipts. This followed a substantial increase in spending of $1.8B (or 14%) in FY2023 relative to the Budget 2022 plan. Still, expense growth is set to rise only moderately going forward. For FY2024 to FY2025, the average annual rate of total spending is forecast at just 0.9%. That is less than the expected rate of inflation plus population growth in both years.

While the increase in expenditures in FY2023 was broad based, health care looks likely to be the primary driver of outlays going forward. Indeed, health spending is expected to come in 6.5% higher in FY2023 than projected in Budget 2022, and increase by a further 7% in FY2024. Some of this will be offset by increased transfers from Ottawa, as Nova Scotia will receive a top-up to the Canada Health Transfer (CHT) as part of the federal-provincial health accord agreed to in February. And while spending on seniors and long-term care increased a whopping 18% in FY2023, some of this was one-time spending that won't be repeated in the coming fiscal year.

Risk Sentiment to Drive Bond Yields in Near-Term

Like most other smaller provinces, we expect Nova Scotia's bond yields to be driven primarily by risk sentiment in the coming months. The province's spreads tightened versus Canada and Ontario to begin 2023 amid positive economic news but have fluctuated during the recent period of financial market volatility.

Nova Scotia bonds are among the ones trading tightest to Ontario among the Maritime jurisdictions. That at least partly reflects Nova Scotia's relatively large, liquid, and diversified borrowing program, and suggests delivery against fiscal blueprint targets should support the province's bond yields.

The authors thank Farjad Khan of Desjardins Economic Studies for his contributions to this report.

TABLE 2
Summary of Fiscal Forecasts

	2022–2023		2023–2024		2024–2025		2025–2026		2026–2027
IN $M (EXCEPT IF INDICATED)	Q2 FY2023	Bud. 2023	Bud. 2022	Bud. 2023	Bud. 2022	Bud. 2023	Bud. 2022	Bud. 2023	Bud. 2023
Total revenues	14,010	14,318	12,911	14,169	13,264	14,348	13,662	14,764	15,026
Total expense	14,259	14,713	13,331	14,820	13,642	14,972	13,956	15,533	15,681
Program spending	13,575	14,032	12,627	14,053	12,908	14,175	13,217	14,693	14,778
Debt charges	684	680.5	704	766.9	734	797.3	740	839.7	902.6
% of total revenues	*4.9*	*4.8*	*5.5*	*5.4*	*5.5*	*5.6*	*5.4*	*5.7*	*6.0*
Consol. & Accounting Adjustments	107	135	1	373	1	160	1	158	155
Budget balance	**-143**	**-259**	**-419**	**-279**	**-377**	**-464**	**-294**	**-611**	**-499**
% of GDP	*-0.3*	*-0.5*	*-0.8*	*-0.5*	*-0.7*	*-0.8*	*-0.5*	-1.0	-0.8
Net Debt, % of GDP	—	*32.5*	*36.9*	*33.6*	*39.2*	*34.8*	*40.0*	*35.8*	*36.2*

Sources: Nova Scotia Ministry of Finance and Desjardins Economic Studies