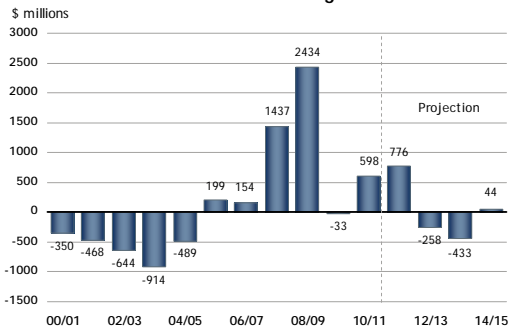


## NEWFOUNDLAND & LABRADOR BUDGET 2012

April 24, 2012

### Drop in revenues, but expenditures stay the course

Newfoundland & Labrador Budget Balance



Source: Newfoundland & Labrador Ministry of Finance, RBC Economics Research

The Newfoundland and Labrador budget, released today, presented what was essentially a “stay the course” expenditure plan in the face of a large projected decline in revenues this year. Interruptions to two major oil field production due to maintenance work will lead to a large drop in offshore oil royalties, while the end of the Atlantic Accord with the federal government will lead to a similarly large decrease in federal transfers; together, these two factors will lower provincial revenues by \$1.1 billion in 2012/13. In contrast, expenditures will continue to grow: program expenditures are expected to increase by 1.7%, practically unchanged from the 1.6% target presented for 2012/13 in last year’s budget. The result is a projected \$258 million projected deficit in 2012/13, representing a significant deterioration from the \$776 million surplus now expected in 2011/12. The provincial budget is projected to remain in deficit in 2013/14 as a result of continued declines in revenue from slower forecasted economic growth; however, the province expects to return to surplus in 2014/15.

#### Budget highlights

**Program expenditures** are expected to be \$6.6 billion in 2012/13, up 1.7% from 2011/12. This includes a 1.7% increase in health expenditures, a 9.0% increase in education expenditures and a 0.3% decline in all other program expenditures. The province’s plan to 2014/15 shows average program expenditure growth of 1.6% per year.

**Revenues** are forecasted to plummet by 10.9%, to \$7.2 billion in 2012/13. This steep decline is the result of a large drop in both federal transfers (down 33.7%, from \$1.6 billion to \$1.1 billion) and offshore royalties (down 20.8%, from \$2.8 billion to \$2.3 billion.) The decline in federal transfers is due to the end of offset payments under the Atlantic Accord, while the drop off in offshore oil royalties will result from maintenance work at two of the province’s major oil projects this summer, which will lead to an estimated 21% decline in oil output this year. This \$1.1 billion revenue gap will be partially closed by a solid 9.2% increase in taxation revenues, driven mainly by a large increase in revenues from corporate taxation. No new revenue-raising measures were introduced in the budget.

**Capital spending** will be \$1.4 billion in 2012/13. Nearly half of this amount appears to be related to the Lower Churchill Project, with \$664 million in projects related to “energy investments.”

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The province's **net debt** is forecast to rise from \$7.8 billion on March 31<sup>st</sup>, 2012, to \$8.5 billion on March 31<sup>st</sup>, 2013. This will push the net debt to GDP ratio to 25.0%, from an estimated 23.9% last year. **Consolidated borrowings** will be \$5.2 billion.

The **economic assumptions** used in budget planning are conservative on the whole. The budget is planning for just 0.1% real GDP growth in 2012, well below RBC's forecast of 2.8%. Even with faster planned growth of 4.1% in 2013 (versus RBC's 3.0%), the fiscal year growth averages to just 1.1%. This offers some upside potential to the revenue forecasts. On the other hand, the budget assumption for the Brent price of crude oil (US\$123.45/barrel) is somewhat optimistic relative to RBC's (US\$116/barrel), which could indicate a risk of revenues coming in lower than planned.

While the planned return to deficits in Newfoundland and Labrador this year is disappointing, it is primarily the result of unusually low revenues. The decline in revenues was the result of two factors: one permanent (the \$540 million drop in federal transfers) and the other transitory (the loss of \$590 million in offshore royalties due to maintenance work.) Without this latter decline, the provincial budget would be in surplus again this year. Moreover, the budget balance in Newfoundland and Labrador is notoriously difficult to forecast, due to the volatility of economic growth in the province and the sensitivity of provincial revenues to commodity prices. Any increase in economic growth (as seems likely) or oil prices relative to the budget assumptions could lead to a substantial improvement in the fiscal results.

## Newfoundland & Labrador fiscal plan

(\$ millions)	Actual	Estimates	Revised	Estimates	Projection	
	2010/11	2011/12	2011/12	2012/13	2013/14	2014/15
<b>Total revenues</b>	8,137	7,343	8,092	7,211	7,189	7,744
Fiscal revenue	7,928	7,124	7,825			
Net income of government business enterprises	210	219	266			
<b>Total expenditures</b>	7,539	7,284	7,315	7,469	7,622	7,700
Program expenses	6,702	6,479	6,525	6,638	6,767	6,834
Debt servicing expenses	837	804	790	831	855	865
<b>Surplus/(Deficit)</b>	598	59	776	-258	-433	44

Source: Newfoundland & Labrador Ministry of Finance, RBC Economics Research

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