Chapter 4: Nova Scotia's Financial Condition

Why we did this work:

- To help Nova Scotians understand the Province's financial results
- To provide independent information on the Province's financial health

Overall comments:

- Unfavourable five-year trend across key sustainability indicators continues
- Some indicators show modest improvement in financial shape in past year
- Interest on debt decreases flexibility in expanding programs or reducing taxes
- Net debt increasing faster than population
- Amount of future revenue needed to pay debt increasing
- Provincial net debt placing increasing burden on economy

What we found:

- Provincial deficit $135 million less than budgeted
- Tax revenue $119 million more than planned in 2014-15 budget
- Expenses were $93 million higher than planned
- Decrease in deficit from prior year due to $451 million increase in provincial tax revenues
- Increased tax revenues in 2014-15 led to favourable results
- Ratio of debt to revenue decreased from $1.47 in 2014 to $1.41 in 2015
- Continuing reliance on federal government equalization payments and other transfers
- Net debt increased by $2.3 billion or 18% over four years
- Government owes $15,944 for each Nova Scotian

4 Nova Scotia's Financial Condition

Background

4.1 One resource in assessing the financial condition of government is the province's consolidated financial statements. The consolidated financial statements provide a snapshot of the province's financial position at its fiscal year end (March 31) and the results of its operations, and changes in both cash flow and net debt for the preceding fiscal year. However, the consolidated financial statements do not provide a complete indication of the province's health nor how well it is performing in relation to its economic and fiscal environment. Although there is information on the economy, including several indicators, in Volume 1 of the Public Accounts, we felt it important to include our own assessment of the indicators of financial condition as part of our reporting to Nova Scotians.

4.2 In prior years, our Office conducted a comparison with other jurisdictions. This year, because not all comparable jurisdictions' public accounts have been released, we have included indicators on Nova Scotia's performance only, including prior year comparisons where appropriate.

4.3 There are numerous indicators that can be used to assess a government's financial condition. The indicators we have included in this chapter are among those recommended for reporting by the Public Sector Accounting Board's Statement of Recommended Practice 4: Indicators of Financial Condition. The statement is not part of generally accepted accounting principles for the public sector, nor is there a requirement for government to implement its recommendations. The indicators reported in this chapter are meant to provide additional information on the province's financial condition, but are not intended as commentary on the financial impact of government policies.

4.4 The Statement of Recommended Practice recommends that, at a minimum, indicators related to sustainability, flexibility and vulnerability are considered. We have included these types of indicators, along with other information we feel is useful in demonstrating the province's financial condition. Definitions of sustainability, flexibility and vulnerability follow, as well as the selection of indicators related to each.

Chapter Objective

4.5 The objective of this chapter is to provide independent information on the province's financial health through reporting on certain indicators of financial condition.

Significant Observations

Overall Financial Condition

Nova Scotia's financial condition improved last year but overall unfavourable five-year trend

4.6 The following table provides an overview of the province's financial performance for the year ended March 31, 2015, and a summary of the financial indicators included in this chapter. As can be seen, the trend in many of the indicators has improved favourably over the prior year. However, sustainability indicators from the past five years show an unfavourable trend.

Type	Indicator	1-year Trend	5-year Trend
Financial Performance	Budget-to-actual Variance	Favourable	N/A
	Actual-to-actual Variance	Favourable	
Sustainability	Net Long-term Debt	Unfavourable	Unfavourable
	Net Debt	Unfavourable	Unfavourable
	Net Debt Per Capita	Unfavourable	Unfavourable
	Net Debt as a Percentage of Total Revenue	Favourable	Unfavourable
	Annual Surplus or Deficit	Favourable	Unfavourable
	Net Debt as a Percentage of Provincial GDP	Stable	Unfavourable
Flexibility	Debt Servicing Costs as a Percentage of Total Revenue	Stable	Stable
Vulnerability	Federal Government Transfers as a Percentage of Total Revenues	Favourable	Stable

Favourable/Unfavourable – represents the direction of indicator; not a comment on performance or policy
Stable – a change of 1% or less
N/A – increase or decrease of this indicator is not considered indicative of either favourable or unfavourable

Financial Performance 2014-15

Budget-to-actual Variance ($ millions)			
Financial Element	**Estimates**	**Actual**	**Variance**
Provincial-source Revenue	$6,700	$6,904	$204
Federal-source Revenue	$3,367	$3,380	$13
Expenses	($10,686)	($10,779)	($93)
Government Business Enterprises (Net Income)	$340	$351	$11
Deficit	($279)	($144)	($135)

4.7 *Budget-to-actual variance* – One measure of financial performance is the extent to which government adhered to the fiscal plan detailed in its budget. For the year ended March 31, 2015, the Province of Nova Scotia estimated a deficit of $279 million. The actual result for the year was a deficit of $144 million, a favourable variance of $135 million. The table above provides an overview of the variance by significant financial element, after consolidation adjustments, that contributed to this positive result.

Tax revenue higher than budget by $119 million

4.8 Provincial-source revenue increased by $204 million from the 2014-15 estimates, due mainly to a $119 million upward adjustment to tax revenue estimates. The upward adjustment to tax revenue estimates is attributed to changes in estimates in consumption and national corporate profits.

4.9 Gross actual expenses were over budget by $203 million. They were offset by cost savings in other areas, resulting in a net reported expense overexpenditure of $93 million. Cost savings were mainly attributed to savings of $89 million in estimated restructuring costs and $13 million in the Department of Municipal Affairs due primarily to Build Canada Fund project delays and general operating savings.

4.10 Gross actual expenses were $203 million over budget due to the following.

- Total increases of $85 million at the Departments of Health and Wellness and Education and Early Childhood Development.
- $40 million over budget at the Department of Internal Services, mainly due to $35 million in environmental remediation costs.
- Economic and Rural Development and Tourism incurred $32 million more in expenses than planned, of which $11.5 is attributed to supporting the Yarmouth Ferry, along with $18 million in the provision for credit losses at Nova Scotia Business Incorporated.
- The Department of Community Services was also over budget by $26 million, the majority of which is due to increasing caseloads and client costs in the Disability Support program.

- Transportation and Infrastructure Renewal was over budget by $20 million primarily due to increased snow removal costs.

4.11 *Actual-to-actual variance* – The following table details variances in revenues and departmental expenses to explain the $533 million change in operating results between March 31, 2014 and March 31, 2015.

Actual-to-actual Variance ($ millions)			
Revenues and Departmental Expenses	**Revenues**	**Expenses**	**Surplus (Deficit)**
2013-14 Deficit	**$10,060**	**$10,737**	**($677)**
Increased Provincial Tax Revenue	$451		
Increased Other Provincial Revenue	$140		
Net Decrease – Other Revenues	($16)		
Increased Economic and Rural Development Expenses		$34	
Increased Education and Early Childhood Development Expenses		$69	
Increased Health and Wellness Expenses		$100	
Decreased Pension Valuation Adjustment		($310)	
Net Increase – Other Expenses		$149	
2014-15 Deficit	**$10,635**	**$10,779**	**($144)**
Change from prior year	**$575**	**$42**	**$533**

Decrease in deficit from prior year due to $451 million increase in provincial tax revenue and $310 million reduced pension expenses

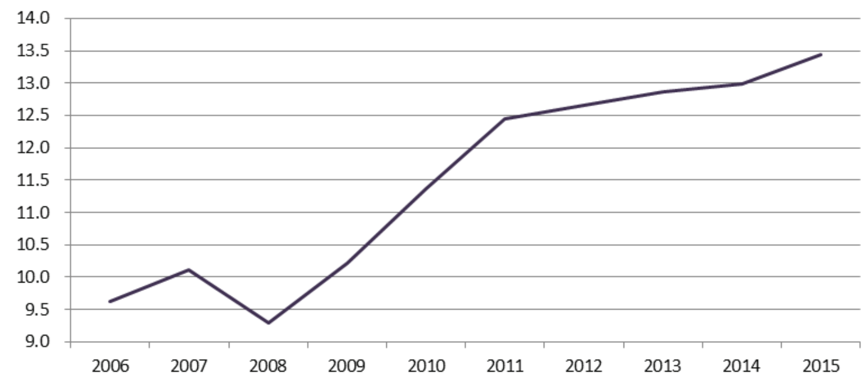
4.12 The province's March 31, 2015 deficit was $144 million. This was a decrease of $533 million over the prior year deficit of $677 million. The more significant variances related to increased provincial tax revenue of $451 million and increased other provincial revenue of $140 million over the previous year. Increases in departmental expenses were offset by the decrease in the pension valuation adjustment. Last year's pension valuation adjustment included a one-time expense of $318 million to reflect the accounting impact of changes to the province's Public Sector Superannuation Plan.

Financial Indicators

Sustainability

4.13 Sustainability measures the ability of a government to maintain its existing programs and services, including maintaining its financial obligations to creditors, without having to introduce revenue and expenditure adjustments such as increased debt or tax rates. Sustainability indicators provide insight into how a government balances its commitments and debts. In the following paragraphs, we discuss the indicators we have selected to assess sustainability.

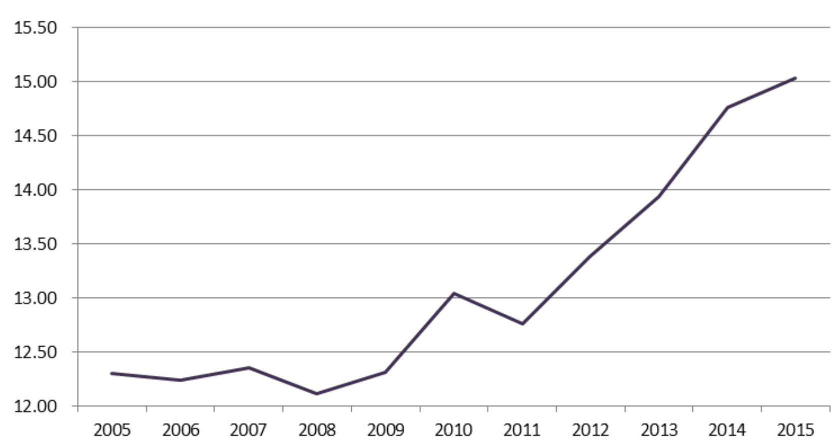
Net Long-term Debt ($ billions)



4.14 *Net long-term debt* – Details of the province's long-term debt is included in Schedule 4 of the March 31, 2015 Public Accounts. Gross long-term debt is $16.8 billion (2014 – $16.4 billion). This includes the debt of all entities in the government reporting entity. The majority of this debt ($15.9 billion, or 95%) is assumed by core government; that is, not through government agencies. Gross long-term debt is offset by sinking fund assets of $3.4 billion.

4.15 We have commented in prior years that the increasing trend in net long-term debt is a significant indicator of fiscal sustainability because the cost of servicing this debt takes priority over program expenses and reduces the ability of government to expand services or reduce taxes. The chart above shows actual growth of net long-term debt over the past ten years, with an increase of approximately $4 billion since 2008.

Net Debt ($ billions)



4.16 *Net debt* – Net debt is the difference between the province's financial assets and its financial liabilities. It is an indication of the government's current obligations that must be funded through future revenues, including taxation. Nova Scotia's net debt is approximately $15 billion.

Net debt increased by $2.3 billion or 18% over four years

4.17 Net debt has increased by 18% or $2.3 billion over the past four years, although the increase of $269 million (2%) over the prior year is a significant improvement over past years' increases. Net debt has grown each year since 2008 except for the year ended March 31, 2011. The surplus of $585 million reduced net debt in that year.

Net Debt per Capita

	2011	2012	2013	2014	2015
Net Debt ($ thousands)	$12,758,315	$13,382,946	$13,942,372	$14,761,747	$15,030,615
% Increase in Net Debt		5%	4%	6%	2%
Population (thousands)	944.5	944.8	942.9	942.7	942.7*
Net Debt per Capita	$13,508	$14,165	$14,787	$15,659	$15,944
% increase in Net Debt per Capita		7%	4%	6%	2%

* *Statistics Canada had not released the 2015 population figures as of September 2015; therefore, the last known population was carried forward for comparative purposes.*

Government owes $15,944 for each Nova Scotian

4.18 *Net debt per capita* – Another indicator of sustainability is net debt per capita. This shows the amount of net debt attributable to each person living in the province. The increasing net debt per capita indicates net debt is increasing at a rate exceeding population growth, and therefore may not be sustainable. Essentially, the indicator shows that the Government of Nova Scotia owes $15,944 for each Nova Scotian for past decisions that resulted in spending exceeding revenues.

4.19 Net debt per capita has increased every year over the past five years since 2011. The indicators show the amount of net debt per capita ranges from a low of $13,508 in 2011 to a high of $15,944 in 2015. Net debt per capita increased 2% during 2014-15.

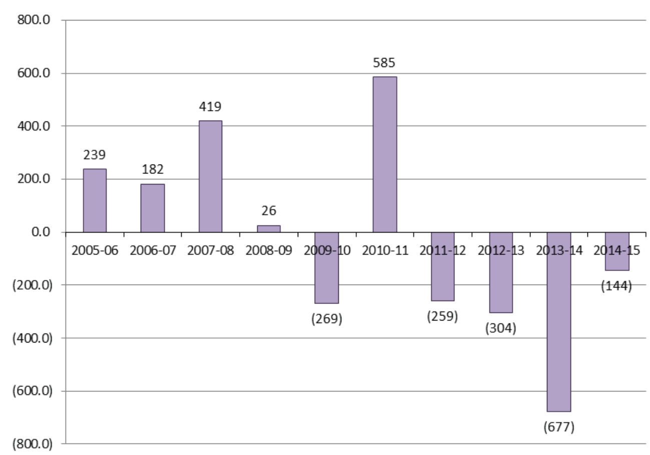
Net Debt as a Percentage of Total Revenue					
Year Ending March 31	**2011**	**2012**	**2013**	**2014**	**2015**
Net Debt ($ millions)	$12,758	$13,383	$13,942	$14,762	$15,031
Total Revenue ($ millions)	$9,919	$9,760	$10,104	$10,060	$10,635
Net Debt/Revenue	129%	137%	138%	147%	141%

4.20 *Net debt as a percentage of total revenue* – Increasing net debt as a percentage of total revenue means it will take longer to repay the debt than it had been in prior years. It also shows that debt is growing faster than revenues. This is a key indicator of sustainability.

Percentage of net debt over total revenue decreased 6% in 2015

4.21 During 2015 the percentage of net debt over total revenue decreased by 6%. This was not as a result of a decrease in net debt but rather due to an increase in total revenue of $575 million. This is a favourable change. In the prior year, there was $1.47 of debt for every $1 of revenue; in the current year this has been reduced to $1.41 of debt for every $1 of revenue.

Annual Surplus or Deficit ($ millions)



4.22 *Annual surplus or deficit* – This annual result indicates the extent to which the government's revenues are more or less than its expenses during the year. A surplus means revenues exceed expenses, while a deficit is a result of expenses exceeding revenues.

4.23 The chart shows there have been significant fluctuations in results over the past ten years. Nova Scotia has been experiencing deficit positions for five of the last ten years. We feel it is important to note that the annual surplus or deficit should be considered in relation to the amount of expenditures. Therefore, we are including the total expenses for the Province in the table below.

Total Expenses					
(in $ billions)	2010-11	2011-12	2012-13	2013-14	2014-15
Total Expenses	9.3	10.0	10.4	10.7	10.8

4.24 There are significant fluctuations in the Province of Nova Scotia's annual results from 2006 to 2015, ranging from a surplus of $585 million in 2011 to a deficit of $677 million in 2014. The more significant deficits have occurred in recent years. During this time, expenses have steadily increased. In 2014, Nova Scotia had its largest deficit of $677 million, although $318 million was due to the one-time pension adjustment noted previously.

4.25 Gross domestic product (GDP) is one of the primary indicators used to measure a province's or country's economy. GDP can be measured by either summing the value of the income generated in an economy (income approach) or by the total dollar value of all goods and services purchased by households and the government (expenditure measure).

4.26 GDP is usually stated as a rate of change in a three-month period over the prior three-month period. An economy with two consecutive periods of reduced growth is said to be in recession. GDP values used in our analysis are expenditure-based.

Net Debt as a Percentage of Provincial GDP					
Year Ending March 31	2011	2012	2013	2014	2015
Net Debt ($ millions)	$12,758	$13,383	$13,942	$14,762	$15,031
Provincial GDP ($ millions)	$37,073	$38,349	$38,214	$39,145	$39,145*
Net Debt/GDP	34%	35%	36%	38%	38%

* *Statistic Canada had not released the 2014 GDP figures as of September 2015. The last known GDP was carried forward for comparative purposes.*

Provincial net debt placing increasing burden on economy

4.27 *Net debt as a percentage of provincial GDP* – Net debt as a percentage of provincial GDP provides insight into the ability of an economy to support government's debt. A higher percentage indicates that a government's debt is becoming an increasing burden on the economy and may not be sustainable. A stable or decreasing percentage shows the growth of the net debt is equal to, or less than, the growth of the economy and is likely sustainable. In theory, a larger economy should be able to absorb a higher amount of government debt. Nova Scotia's net debt as a percentage of provincial GDP has consistently increased to its highest rate in the past five years.

Flexibility

4.28 Flexibility describes the extent to which a government can change its debt burden or raise taxes within its economy. Increasing debt and taxation reduces flexibility and the government's ability to respond to changing circumstances. Assessing flexibility provides insights as to how government manages its finances. The following indicator has been selected to assess flexibility.

Debt Servicing Costs as a Percentage of Total Revenue					
Year Ending March 31	**2011**	**2012**	**2013**	**2014**	**2015**
Debt Servicing Costs ($ millions)	$866	$863	$921	$886	$896
Total Revenue ($ millions)	$9,919	$9,760	$10,104	$10,060	$10,635
Debt Servicing Costs as a % of Total Revenue	9%	9%	9%	9%	8%

4.29 *Debt servicing costs-to-revenues* – The ratio of debt servicing costs-to-revenues indicates the amount of current revenue that is required to service debt costs arising from past borrowing decisions and, as a result, is not available for current and future programs and services. Debt servicing costs are variable only to the extent they fluctuate with the amount of debt issued. However, once debt is issued, interest payments on that debt are a fixed cost of government and are its first commitment. Failure to pay interest impacts the ability to raise future debt, and can also increase government's borrowing rate. As debt increases, government is less able to respond to economic changes.

Percentage of revenue needed to pay interest on debt at lowest point in five years

4.30 The proportion of debt servicing costs-to-revenues indicates the amount of current revenues that are required to service past borrowing decisions and, as a result, are not available for current and future programs and services. In Nova Scotia, this ratio has improved from 9% in 2014 to 8% in 2015, indicating that debt servicing costs have increased at a lower rate than revenue in the past year.

Vulnerability

4.31 Vulnerability indicators measure the amount government is dependent on sources of revenue outside its control and its exposure to risks which might affect government's ability to meet its commitments. The lower government's own-source revenue, the more it relies on fiscal decisions of others.

Federal Revenue as a Percentage of Total Revenue					
Year Ending March 31	**2011**	**2012**	**2013**	**2014**	**2015**
Federal Revenue ($ millions)	$3,212	$3,179	$3,263	$3,392	$3,380
Total Revenue ($ millions)	$9,919	$9,760	$10,104	$10,060	$10,635
Federal Revenue as a % of Total Revenue	32%	33%	32%	34%	32%

Continuing reliance on federal government equalization payments and other transfers

4.32 *Federal government transfers as a percentage of total revenues* – This indicator demonstrates the level of federal government transfers compared to total government revenues. The higher the percentage, the more reliance the provincial government puts on receipt of funds from the federal government. These transfers are dependent on policy decisions at the federal level and outside the control of the provincial government. This ratio has remained stable over the past five years with a marginal decrease in 2015.

Sources:

1. *Nova Scotia – Public Accounts for March 31, 2006 – March 31, 2015*
2. *Statistics Canada – Gross domestic product, expenditure-based, by province and territory (2008-2013)*
3. *Statistics Canada – Population by year, by province and territory (July 2008 – July 2014)*

Note: Income from Government Business Enterprises (GBE) has been included in the calculation of own-source and total revenue.