

Economics

PROVINCIAL BUDGET BRIEFS

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Andrew Grantham andrew.grantham@cibc.com

Tom Bognar, CFA tom.bognar@cibc.com

Prince Edward Island budget 2023

Yesterday's budget from Prince Edward Island detailed further spending increases and changes to the tax structure that will see the deficit widen slightly this year. The \$97.6mn deficit anticipated for the current fiscal year is equivalent to roughly 1% of nominal GDP and is up from a revised estimate showing a \$66.2mn shortfall in 2022/23. Total cash requirements are increasing year-over-year by about \$78mn, reaching \$374mn, due to the wider operating deficit and higher capital spending plans. The province is electing to fund that by increasing both short- and long-term funding, with the latter expected to be \$50mn higher than last year at \$250mn.

Table 1: Summary of fiscal position: (C\$millions)

Fiscal measure	2021/22 Actual	2022/23 22 Budget	2022/23 23 Budget	2022/23 Change	2023/24 23 Budget	2024/25 23 Budget	2025/26 23 Budget
Revenue	2,653	2,569	2,840	270	2,995	3,148	3,290
Provincial sources	1,619	1,556	1,760	204	1,780	1,885	1,970
• % change	15.9	0.0	8.7	8.7	1.2	5.9	4.5
Federal source	1,034	1,013	1,080	67	1,215	1,263	1,320
Expenditures	2,569	2,662	2,906	244	3,093	3,206	3,321
Programs	2,349	2,429	2,655	227	2,809	2,904	3,002
• % change	8.8	1.9	13.0	11.0	5.8	3.4	3.4
Public debt interest	121	131	143	12	163	172	183
Amortization of tangible capital assets	99	103	108	5	121	130	137
Consolidated budget balance	83.8	-92.9	-66.2	26.7	-97.6	-58.0	-31.5

PEI economy still strong

Prince Edward Island saw real GDP growth of 2.9% in 2022. While that's slightly below the national average of 3.4%, it should be remembered that PEI saw a much smaller decline in activity during the pandemic and a stronger initial recovery. The 7.9% advance in real GDP during 2021 was the highest among Canadian provinces and well above the 5.0% national average. Exports were strong during 2022 and have risen even further in the first quarter of 2023. While overnight tourist stays have moved above pre-pandemic levels, those undertaken by non-resident travellers still have room to recover. The 3.6% increase in the Island's population during 2022 was the strongest in the province's history, adding to potential labour force growth but also creating extra demands on services such as health and education.

Moderate deficit projected, slimming later

Like most other provinces, PEI saw much higher than expected revenues during the last 2022/23 fiscal year, with that windfall mainly used to support additional spending to help residents with growing affordability difficulties. Revenues are estimated to have been \$270mn higher than initially budgeted for, with spending \$244mn greater. The \$66mn deficit now projected for the 2022/23 fiscal year is roughly two thirds the \$93mn shortfall that was initially expected.

For the current 2023/24 fiscal year, own source revenue growth is expected to increase by a slim 1.2% despite a still-solid economic backdrop. The province is increasing the basic personal amount, raising the threshold for low-income tax reduction and will be moving to a five bracket income tax system beginning in 2024, with those measures coming at a cost

of \$14mn. While own source revenues are expected to rise only modestly compared with the prior year, a bump up in federal transfers (to \$1.215bn from \$1.080bn) will support overall revenues.

On the spending side, further commitments in key areas such as health and education see program spending rising by a further 5.8% in 2023/24 compared to the prior year. That leaves the deficit expected to widen slightly to \$98mn, which would be roughly 1% of provincial nominal GDP.

The medium-term forecasts show stronger own-source revenue growth and more moderate increases in spending for the years ahead. That would see the deficit slimming to \$58.0mn in 2024/25 (0.6% of nominal GDP) and \$31.5mn in 2025/26 (0.3% of GDP).

Short- and long-term borrowing slightly increasing

With the forecasted improvement in the deficit for fiscal year 2022/23, along with lower net borrowing requirements on behalf of Crown Corporations, total cash requirements fell from \$332mn in last year's budget to a projected \$295mn by year-end. As a result, the province altered its borrowing plans and elected to increase its short-term funding/liquidity reserves to \$95mn, up from \$82mn previously planned. At the same time, long-term borrowing plans were reduced by \$50mn and finished the year at \$200mn.

The province raised that \$200mn in a single transaction which was completed in January of this year, a new 10yr benchmark with a 3.75% coupon maturing December 2032. That deal placed the total number of bonds outstanding for the province at 17 with a value of \$2.565bn. Despite a higher coupon than their last few deals, it was still lower than their weighted average coupon of 4.03%. That is due to the fact that most of their other bonds outstanding were issued between 2000 and 2015 when interest rates were higher. As a result, the province still has the highest weighted average coupon amongst its provincial peers. For example, the province's next bond maturing is a \$60mn bond due this December with a coupon of 8.50%. However, the budget states that this maturing bond will not be re-financed with new debt. Instead, it is being financed by proceeds from the sinking fund.

For the current fiscal year, the province's total cash requirements are increasing year-over-year by about \$78mn, reaching \$374mn. That is mainly due to the higher deficit forecast, higher capital spending, as well as higher net borrowings on behalf of Crown Corporations. The province is electing to fund that through both short- and long-term funding again. The former will be increasing to \$124mn, from \$95mn last year, while the latter will be up \$50mn from last year to \$250mn.

Table 2: Borrowing requirements (C\$millions)

Borrowing requirements	2022/23 Forecast	2023/24 Estimate
Consolidated (surplus)/deficit	66	98
Capital adjustments	140	187
Sinking funds earnings/provisions	24	23
Pension transfers/accruals	31	5
Borrowing On Behalf of Crown Corp	23	50
Net financial requirement	284	363
Maturities & calls	11	11
Total	295	374

Table 3: Sources of funding (C\$millions)

Sources of funding	2022/23F	2023/24E
Short-term paper	95	124
Bonds and MTNs	200	250
Total	295	374
Net new issues: Bonds & MTNs	200	250

Capital plans are increasing

The province's capital plan is expected to be higher this year at \$308mn, up from \$248mn last year. The three key areas of focus highlighted in the budget address were housing, healthcare and affordability. As a result, the largest increase year-over-year in dollar terms will be in Housing, Land and Communities, which jumps almost three-fold to \$65mn.

Meanwhile, the largest decrease will be in Transportation and Infrastructure which drops \$13mn to \$80mn. Despite the drop, that line item is still the largest spend for the province in terms of capital assets acquired.

That higher capital spending coupled with an increase in the deficit forecast translates into higher borrowing, placing net debt-to-GDP for 2023/24 at 28.8%. That is an increase from the forecasted 27.6% this past year. Looking ahead, the three-year fiscal plan sees that ratio increasing again to 29.5% in 2024/25, then slightly decreasing to 29.3% the following year (i.e. 2025/26). The reason for the forecasted increase next year to 29.3% is that net debt, as a result of higher capital spending and not a higher deficit, is proportionately outpacing GDP growth.

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