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BUDGET BALANCE TARGET PUSHED BACK A YEAR

Highlights

- The Prince Edward Island (PEI) government is estimating a deficit of $34.7 million (0.6% of GDP) in fiscal 2014-15. The budget plan calls for the deficit to narrow to $19.9 million (0.3% of GDP) in fiscal 2015-16 before returning to a surplus position in fiscal 2016-17. This pushes the deficit reduction timetable back by one year relative to what was presented in last year's budget.
- Expenditure restraint and an acceleration in economic growth will be relied upon to lead the Province back to balance. Growth in total spending will average 0.6% over the next three fiscal years. Total revenues are assumed to rise 2.2% on average over the same time period.
- The budget introduced a new tobacco tax. The tax on a carton of 200 cigarettes will rise by $5 while the tax on 200 grams of fine tobacco will increase by $8. Recently, the government also introduced the PEI Generic Drug Plan and amendments to its income tax legislation to provide relief for low-income earners.

Finance Minister Allen Roach tabled his first budget today, outlining a three-year fiscal plan that returns the Province to a budget balance position next year and sees the debt burden steadily decrease. The path to balance has been pushed back by one year, but this was already signaled by the government in its election platform in April. A deficit of $34.7 million (0.6% of GDP) is now estimated for fiscal 2014-15, which is $5 million lower than the forecast in last year's budget. The fiscal plan calls for a steady improvement in fiscal position with the deficit forecast to narrow to $19.9 million (0.3% of GDP) in fiscal 2015-16, before surpluses of $11.9 million and $44.1 million are projected in the final two years of the plan.

Government to hold the line on spending

The path to balance counts on lean spending targets. Indeed, total expenditures (-0.4%) are forecast to decline for a second consecutive year in fiscal 2015-16. The two largest spending departments – health and education and early learning – are both slated to record moderate 1% increases in spending in fiscal 2015-16. As such, spending in all other areas is projected to decline 2% this fiscal year. In the final two years of the plan growth in total spending is assumed to average modest gains of 1.1%.

PRINCE EDWARD ISLAND GOVERNMENT FISCAL POSITION

[C$ Millions, unless otherwise indicated]

	2015 Budget			
Fiscal year	14-15	15-16	16-17	17-18
Revenues	**1,641**	**1,649**	**1,699**	**1,750**
% change	-3.0	0.5	3.1	3.0
Provincial*	993	1,016	1,047	1,078
% change	-4.5	2.3	3.1	3.0
Federal transfers	648	633	652	672
% change	-0.6	-2.3	3.0	3.0
Expenditures	**1,675**	**1,669**	**1,687**	**1,706**
% change	-3.6	-0.4	1.1	1.1
Program spending	1,481	1,476	1,488	1,500
Debt charges	129	127	130	137
Amortization	66	66	69	69
BUDGET BALANCE	**(34.7)**	**(19.9)**	**11.9**	**44.1**
% of GDP	-0.6	-0.3	0.2	0.7
Net Debt*	**2,149**	**2,177**	**2,165**	**2,111**
% of GDP	36.0	35.2	33.7	31.6

Source: 2015 Prince Edward Island Budget and Public Accounts.
*Includes own source revenue, net consolidated surplus of Crown Corporations and revenue for capital assets.

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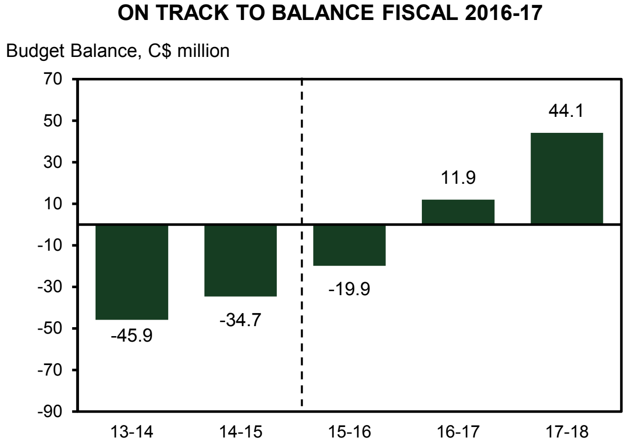
Despite the tight leash on spending, the government did highlight its new PEI Generic Drug Plan that will be unveiled and put into place in October. The new plan follows through on an election promise, and will reduce the cost burden for those without a drug plan by capping payments at less than $20. The new measure is estimated to cost $4 million annually.

Province is counting on strong economic growth

The government assumes a noticeable uptick in economic activity in the coming years, with real GDP growth estimated at 2.7% in 2015 and around 2% in 2016-17. This follows a modest economic performance in 2014 (+1.3% at basic prices). As such, nominal GDP growth is also expected to receive a lift over the fiscal forecast with gains of 3.5%-3.9% projected annually. This improved economic backdrop is expected to translate to an increased revenue-intake for the province. The government's economic assumptions are more bullish than our own and may represent a downside risk to the forecast.

Despite this relatively rosy economic outlook, the government is only assuming a 0.5% increase in revenues in fiscal 2015-16. Provincial revenues are slated to increase 2.3% this year – buoyed by a 4.1% increase in tax receipts. Personal income taxes are forecast to increase 5.8% in fiscal 2015-16. Health and tobacco taxes are expected to surge more than 6%, in line with the tobacco tax increase which raises the tax per cigarette by 2.5 cents. Federal transfers are projected to decline 2.3% this year, restricting total revenue intake in fiscal 2015-16. The final two years of the fiscal plan estimate total revenue growth at around 3%.



Source: 2015 Prince Edward Island Budget and Public Accounts.

ECONOMIC ASSUMPTIONS
[Annual percent change unless noted otherwise]

	Forecast		
	2015	2016	2017
Real GDP	2.7	2.1	2.0
Nominal GDP	3.5	3.9	3.9
Employment	0.5	1.1	1.1
Personal Income	1.6	3.2	3.3
Retail Sales	2.0	3.5	2.9

Source: 2015 Prince Edward Island Budget/Conference Board of Canada.

The government also highlighted how it recently tabled legislation to change its *Income Tax Act* that will provide relief to low income earners. The proposed changes will increase the value of the basic, spouse and child tax credits by $50. A new $250 senior credit will also be introduced. The income threshold at which full credit amounts can be realized has been increased to $17K from $15K.

Capital spending to pare back

Net debt is forecast to peak in fiscal 2015-16 at $2.177 billion but is expected to decline over the remainder of the fiscal plan. However, because of the expected pick-up in economic growth, the net debt-to-GDP ratio is projected to fall steadily to 31.6% by fiscal 2017-18 from 36% in fiscal 2014-15. Net capital spending is pegged at $74.5 million this fiscal year, and is estimated at $68.7 million in fiscal 2016-17 and $59 million in fiscal 2017-18.

Bottom line

The government has pushed back its balanced budget target by one year to fiscal 2016-17. The fiscal plan continues to hold the line on spending and counts on strong economic growth to help guide the Province back to balance. The relatively strong economic forecast assumptions imply a downside risk to the revenue targets, but the government's recent track record of tight expenditure management should help keep the Province on track to balance its books.

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