Chapter 2
Nova Scotia's Finances from the 2023 Public Accounts

Key Messages

- Nova Scotia's economy and finances have shown improvements over the past five years:
  - Operating surpluses in four of the past five years
  - Net debt to GDP ratio improved
- Dependency on federal government transfers has decreased since its peak due to COVID-19 funding in 2020-21
- Provincial source revenue was $1.9 billion higher than budget, and expenses were $1.33 billion higher than budget
- Province ended 2022-23 with a surplus of $115.7 million

Why We Did This Audit

- To provide important information to Nova Scotians on the Province's finances and promote discussion

Financial Condition of the Province of Nova Scotia

Government's financial condition can be assessed by ratios and indicators of sustainability, flexibility, and vulnerability. These indicators are suggested by CPA Canada's independent Public Sector Accounting Board.

Sustainability indicators show the Province's ability to maintain existing services and financial requirements without needing to increase revenues or debt

- 2022-23 operating surplus of $115.7 million was $621.9 million higher than the budgeted deficit of $506.2 million and represents the second largest budget to actual change in five years
- Net debt increased $2.8 billion to $17.8 billion since 2018-19, with an upward trajectory in the growth rates year over year
- Net debt to GDP ratio of 31.7% improved from the prior year ratio of 33.1%
- Overall: while indicators have fluctuated over the past five years, recent operating surplus and decreasing net debt to GDP ratio show improvement

Flexibility indicators show the Province's ability to increase revenues or debt borrowings within its economy

- Interest on unmatured debt has increased by $26 million from the 2021-22 low of $549 million as a result of increasing interest rates, even though unmatured debt decreased in 2022-23
- In 2022-23, provincial source revenue to GDP ratio worsened, rising by 1.6 percentage points to 19.1%, the highest level of the past five years
- Overall: flexibility indicators have fluctuated over the past five years

Vulnerability indicators show the Province's reliance on revenues outside of its control

- Dependency on federal government transfers saw the largest year-over-year decrease in the five-year trend, falling by 4 percentage points to 31.3 per cent. This decline is primarily due to COVID-19 funding that did not re-occur in 2022-23
- Overall: federal transfers as a percentage of total revenues have improved, indicating less reliance on outside revenues, with 2022-23 being on the low end of the five-year trend. However, federal transfers represent almost a third of the Province's revenues

Selected Financial Highlights

Revenue:

- At $10.7 billion, provincial source revenue was $1.9 billion higher than budgeted with $929 million resulting from prior years' adjustments
- Personal income tax revenue of $3.6 billion was higher than both the budgeted and prior year amounts and has risen 35% since 2018-19
- Harmonized sales tax revenue of $2.4 billion was higher than both budget and prior year amounts and has risen 30% since 2018-19
- Corporate income tax revenue of $729 million was the peak of the five-year trend and $193 million higher than budgeted
- Net income from government business enterprises reached a five-year high of $465 million, $45 million higher than budgeted

Questions Nova Scotians May Want to Ask

1. Why was the 2022-23 ending surplus so much more than expected?
2. What will happen to the Province's finances if the Bank of Canada continues to raise rates?
3. How has inflation impacted the Province's finances?
4. What does the decrease in the net debt to GDP ratio mean for me?
5. Why is Nova Scotia's net debt to GDP ratio the second highest of the Atlantic Provinces, behind only Newfoundland?

2 Nova Scotia's Finances from the 2023 Public Accounts

Purpose

2.1 The purpose of this chapter is to inform Nova Scotians on the Province's finances and to promote discussion.

2.2 In this chapter, we look at numbers from the perspective of sustainability, flexibility, and vulnerability and provide information on revenues over the past five years to provide insight into the Province's financial condition.

Limitations

2.3 We are not assessing or commenting on the financial decisions made by Government or the effectiveness of those decisions. The information presented below is only part of the story and does not consider such factors as policy decisions, actual programs and services, inflation, performance of the provincial economy, and other elements that may impact revenues and expenses. Certain figures and information in this report including information on entities not consolidated in the Province's financial statements is not audited. Additional information, including economic highlights, is presented in the Financial Statement Discussion and Analysis section in Volume 1 of the 2023 Public Accounts of Nova Scotia where there are more than 50 pages of detailed analysis and explanation.

Financial Indicators – What They Show

Indicators are showing both favourable and unfavourable trends

2.4 There are various indicators that can be used to assess the Province's financial condition. The indicators 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 indicators reported 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 or fiscal management.

2.5 The Statement of Recommended Practice recommends that, at a minimum, indicators related to sustainability, flexibility, and vulnerability be considered. We have included these indicators, along with other information we feel is useful in demonstrating the Province's financial condition. These indicators assist users of the Province's consolidated financial statements in interpreting the financial information.

2.6 The financial indicators presented in this chapter provide an overview of the Province's financial performance for the five-year period ending March 31, 2023, and are summarized in the table below as well as in the 2022-23 Public Accounts.

Financial Highlights	
Indicator	**Five-Year Trend**
Sustainability	
Annual surplus or deficit	Favourable
Net debt	Unfavourable
Net debt to GDP	Favourable
Unmatured Debt	Unfavourable
Flexibility	
Interest on unmatured debt	Favourable
Provincial source revenue to GDP	Unfavourable
Vulnerability	
Federal government transfers as a percentage of total revenue	Favourable

2.7 Individual indicators show a range of impacts on sustainability and flexibility. Results also show the Province appears to be less vulnerable with a lower reliance on federal revenues.

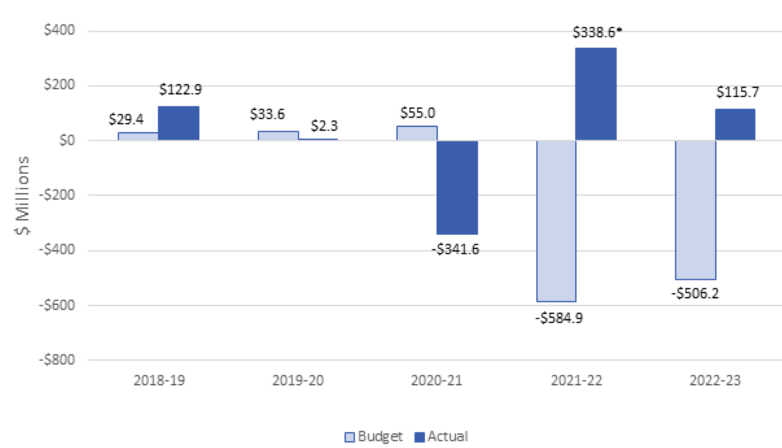
Sustainability

2.8 Sustainability measures the ability of a government to maintain its existing programs and services, including its financial obligations to creditors, without increasing debt or tax rates. Sustainability indicators provide insight into how a government balances its commitments and debts.

The Province reported an annual operating surplus of $115.7 million for 2022-23

2.9 The annual surplus/deficit measures the extent to which revenues cover expenses. A surplus occurs when revenues are greater than expenses. A deficit occurs when expenses are greater than revenues.

Annual Surplus/Deficit – 2018-19 to 2022-23 ($ Millions)



** See 2022-23 Public Accounts, Volume 1, Note 2: 2021-22 value was restated from $350.9M to $338.6M.*
Source: 2022-23 Public Accounts

2.10 Reported results in 2022-23 show significant improvement over the initial 2022-23 budget estimates for the second year in a row. The resulting surplus of $115.7 million was $621.9 million (2021-22 - $923.5 million) higher than the budgeted deficit of $506.2 million, however it was $222.9 million lower than the prior year's surplus of $338.6 million. Although this year's budget to actual change was not as large as in 2021-22, the difference remains significant, and represents the second largest budget to actual change in five years.

2.11 The 2022-23 swing from budgeted deficit to actual surplus was mainly driven by a $1.9 billion increase in Provincial source revenues including:

- Increase in major tax revenues of $763 million from budget:

    - Personal income tax revenue increased $349 million
    - Harmonized sales tax revenue increased $221 million
    - Corporate income tax revenue increased $193 million

These increases were mainly as a result of the Provincial economy continuing to rebound stronger than anticipated; higher taxable income and projected yield rates (discussed later in the chapter); and greater residential housing investment and consumer expenditures (discussed later in the chapter).

- Prior years' adjustments (PYAs) of $929 million added to major tax revenues. PYAs are not budgeted. They are recorded in the current year as actual or more current information becomes available and impact the accounting estimates for tax revenues recorded in prior years. PYAs are discussed in further detail later in this chapter.

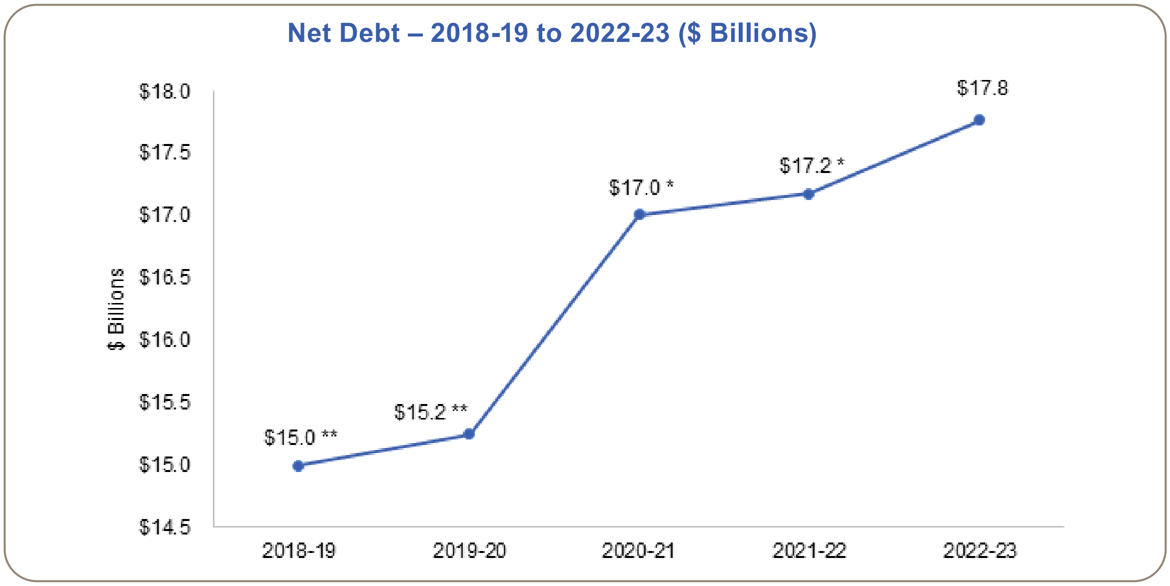
- Increased revenues were offset by a $1.33 billion increase in expenses, some of which was through use of additional appropriations, which are discussed in Chapter 1 of this report.

The Province's net debt increased $2.8 billion since 2018-19

2.12 Net debt measures the degree to which the Province's financial assets cannot cover its liabilities. As the chart below shows, net debt has been on an upward trend, increasing by $2.8 billion since 2018-19.

2.13 Net debt increased significantly in 2020-21 to $17 billion largely due to the impacts of COVID-19 and additional capital spending that year. Net debt in 2020-21, presented below, was also affected by the adoption of a new accounting standard, PS 3280, *Asset Retirement Obligations* in 2022-23. As a result of this new Canadian public sector accounting standard that provides guidance on reporting of liabilities arising from legal obligations associated with the retirement of certain tangible capital assets, 2020-21 net debt was restated from $16.4 billion to $17.0 billion.

2.14 Net debt has continued to rise, reaching $17.8 billion in 2022-23. The increase in net debt from 2021-22 to 2022-23 is partially accounted for through $740.1 million in net tangible capital asset acquisitions, offset by the $115.7 million surplus, and $34.8 million in net remeasurement gains due to the adoption of another accounting standard, PS 3450, *Financial Instruments*. This new standard, which came into effect on April 1, 2022, establishes standards for recognizing, measuring, presenting and disclosing financial instruments and foreign currency transactions.



** See 2022-23 Public Accounts Volume 1, Note 2: 2020-21 value was restated from $16.4B to $17.0B, and 2021-22 value was restated from $16.6B to $17.2B.*
*** Years 2018-19 and 2019-20 have not been restated for the impacts of PS 3280, Asset Retirement Obligations*
Source: 2022-23 Public Accounts

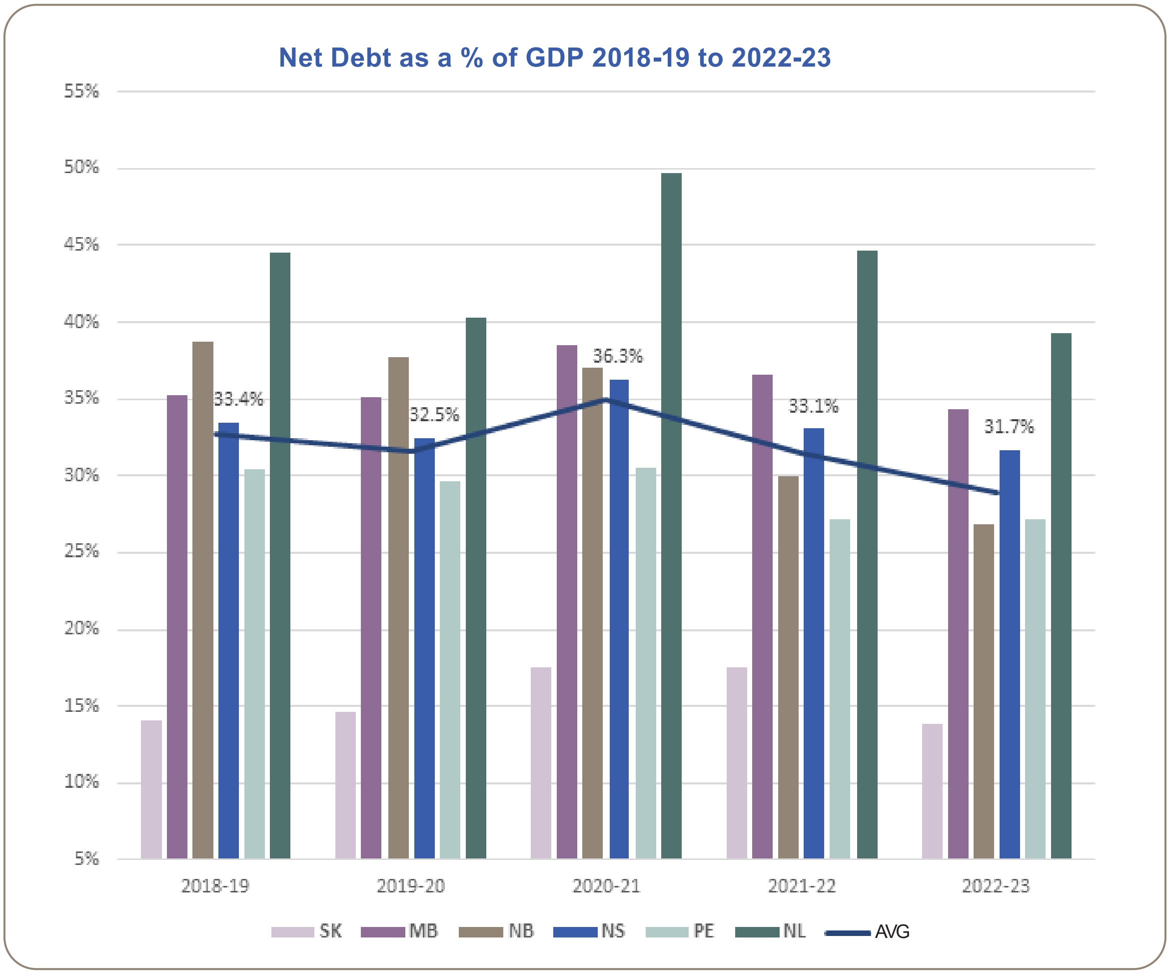
The Province's net debt to GDP ratio has improved over the past five-year period

2.15 Gross domestic product (GDP) is the amount of value added from production of all goods and services within the Province in a given year and is one of the primary measures used to evaluate the economic condition of a province or country.

2.16 The net debt to GDP ratio is used to assess the Province's ability to pay its financial obligations and render services. A low ratio indicates a level of economic output that supports debt repayment. The higher the ratio, the more difficult it may be for the Province to pay its debt while maintaining the same service levels and tax rates.

2.17 The following chart shows that Nova Scotia's net debt to GDP ratio has fluctuated slightly year over year but the trend over the past five years has remained consistent. The high of 36.3 per cent in 2020-21 was the result of COVID-19 impacts. Since then, the ratio has decreased back to pre-COVID-19 levels and was 31.7 per cent in 2022-23, falling 1.4 percentage points from 2021-22. This improvement is an indication that the Province is in a better position to pay back its debts than it was before and during the pandemic.

2.18 The chart shows Nova Scotia's net debt to GDP ratio against other Atlantic provinces as well as Saskatchewan and Manitoba, all of which were chosen for comparison due to either their geographic location or their similar population sizes. While the percentages are not strictly comparable between provinces due to accounting and reporting differences, the average based on the data included in the chart reveals since 2020-21, Nova Scotia, similar to others, is following the downward trend but Nova Scotia is reporting a ratio above the average.

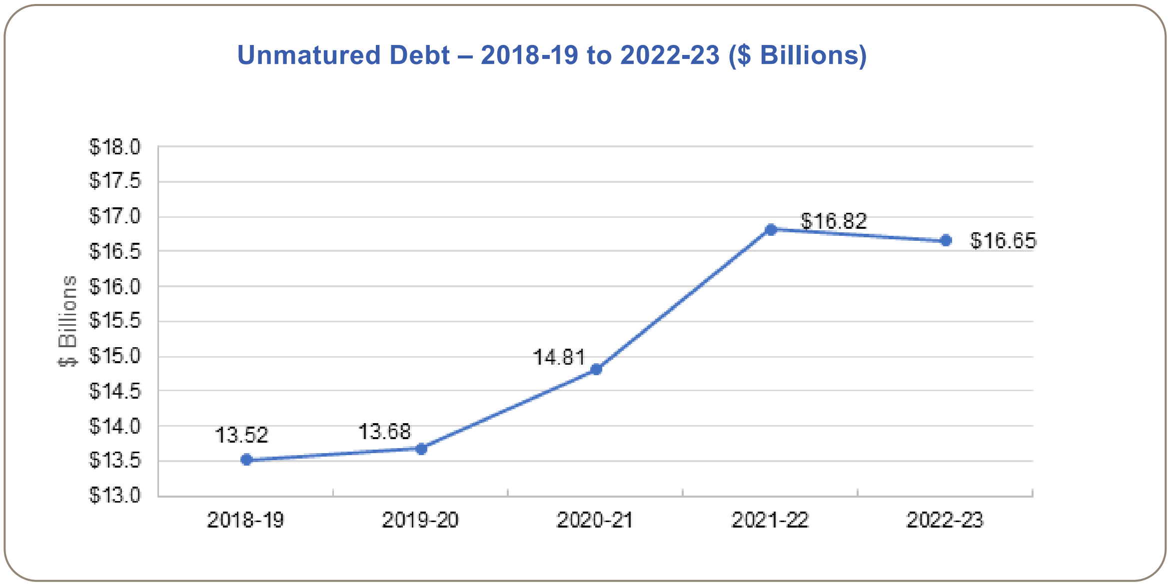


Source: 2022-23 Public Accounts of Saskatchewan, Manitoba, New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland

The Province's unmatured debt decreased by $170 million to $16.65 billion in 2022-23

2.19 The Province's unmatured debt is primarily made up of long-term debentures and various loans. It includes new debt issuances and those from prior years.

2.20 Unmatured debt decreased $170 million from $16.82 billion in 2021-22 to $16.65 billion in 2022-23 and has increased $3.13 billion since 2018-19.



Source: 2019-20 to 2022-23 Public Accounts

2.21 On April 1, 2022, the Province adopted a new accounting standard issued by the Public Sector Accounting Board (PSAB), PS 3450, *Financial Instruments*. Under this new standard, the Province's sinking fund assets, which are an accumulation of assets set aside to repay a loan when it becomes due, are required to be presented separately from unmatured debt as financial assets. Under the previous accounting standards, the Province's sinking fund assets were included within unmatured debt, reducing the liability. Netting of sinking funds is no longer permitted. The 2021-22 reported amount has been reclassified to reflect this accounting standards change, increasing the value of unmatured debt by $1.97 billion from $14.85 billion to $16.82 billion. The chart above presents amounts for 2020-21 and prior years as reported in the financial statements for those years, net of sinking fund assets.

Flexibility

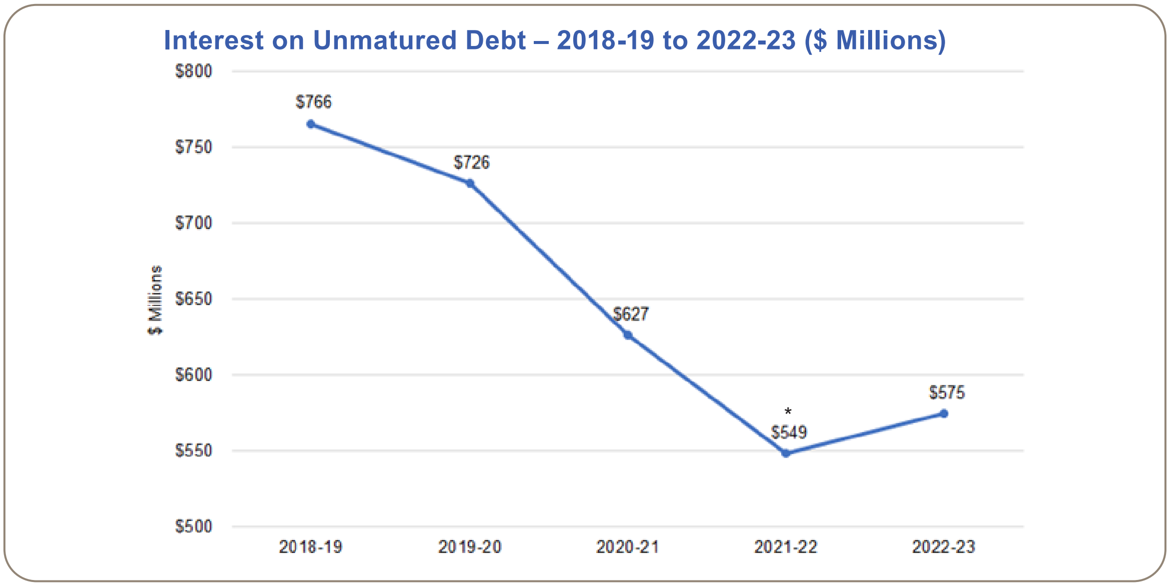
The Province's annual interest on unmatured debt increased $26 million in 2022-23

2.22 Flexibility is the degree to which a government can change its debt or tax burden on the economy to meet its existing financial obligations. Flexibility provides insights into how a government manages its finances. Increasing debt obligations and interest costs reduce a government's future flexibility and its ability to respond to changing circumstances.

2.23 Interest on unmatured debt includes interest on outstanding debentures, loans, capital leases and other costs related to debt financing. Higher debt servicing costs mean the Province is using more of its revenue to pay for interest and is therefore not able to use that money to provide services or reduce taxation. Lower debt servicing costs allow the Province greater flexibility to provide its services and meet financial commitments.

2.24 Interest on unmatured debt has been decreasing since 2018-19 but reported a slight increase in 2022-23. The slight increase is a result of rising interest rates. During 2022-23, the Bank of Canada increased its target for the overnight rate (or "Policy Interest Rate") from 0.5 per cent to 4.5 per cent. This rate is the starting point for setting other interest rates in the Canadian economy (for example interest rates on loans, credit cards, mortgages) and therefore affects the debt servicing costs of the Province.

2.25 The interest on unmatured debt for 2022-23 was $575 million; an increase of $26 million from a five-year low of $549 million in 2021-22.

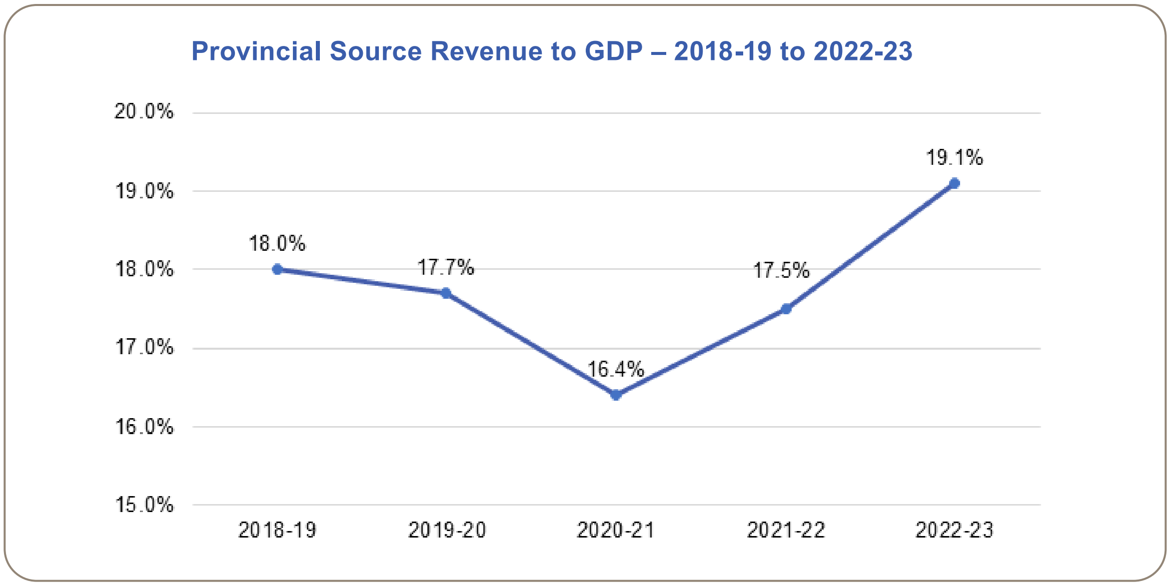


** See 2022-23 Public Accounts, Volume 1, Note 2: 2021-22 value was reclassified from $576M to $549M, due to adoption of PS 3450, Financial Instruments.*
Source: 2019-20 to 2022-23 Public Accounts

Provincial source revenue to GDP worsened in 2022-23, increasing to 19.1%

2.26 Provincial source revenue as a percentage of GDP shows the extent to which the government is leveraging funds from the provincial economy collected through taxation, user fees, and other revenue sources it controls. A high taxation burden may make a jurisdiction less competitive and limit a government's ability to increase own-source revenues. Increases in this ratio may reduce future flexibility. This indicator can help a government determine the extent to which it can access provincial source revenues in the future.

2.27 Provincial source revenue as a percentage of GDP increased to 19.1 per cent in 2022-23, which is 1.6 percentage points higher than 2021-22. The chart shows that the demands on the provincial economy are increasing and are at the highest level in the past five years.



Source: 2022-23 Public Accounts

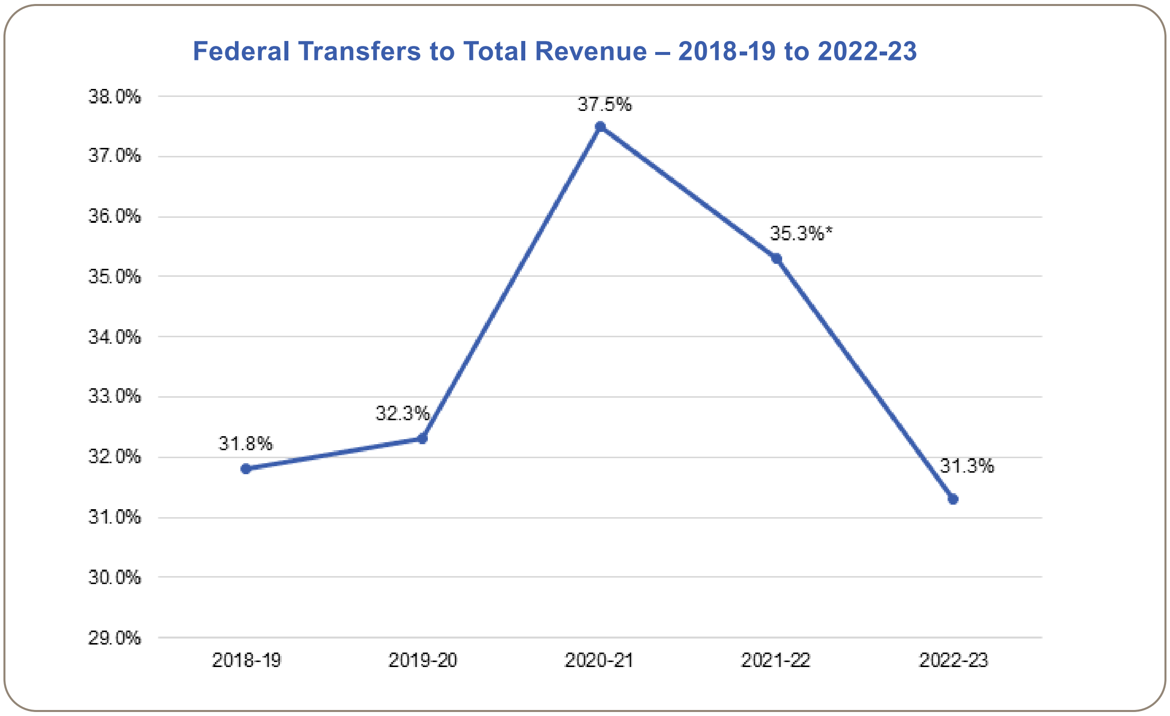
Vulnerability

2.28 Vulnerability indicators measure a government's dependency on sources of revenue outside its control and its exposure to risks which might affect a government's ability to meet its commitments. The more a government relies on revenue from other sources, the more dependent it is on the fiscal decisions of others.

Dependency on federal government transfers has decreased since the COVID-19 funding peak in 2020-21

2.29 As illustrated below, Nova Scotia continues to rely on federal government equalization payments and other transfers. Almost $1 in every $3 of the Province's revenue comes from the federal government.

2.30 The percentage of federal transfers to total revenue has returned to its pre-pandemic levels. The ratio of federal transfers to total revenue decreased 4 percentage points from the previous year to 31.3 per cent. This decline is attributable to provincial source revenue growing at a faster rate than federal transfers and the reduction of federally provided COVID-19 funding. The 2020-21 spike shown below was driven by COVID-19 funding received that year in response to the pandemic.



** See 2022-23 Public Accounts, Volume 1, Note 2: 2021-22 value was reclassified from 35.2% to 35.3% due to adoption of PS 3450, Financial Instruments.*
Source: 2022-23 Public Accounts

Revenue Highlights

2.31 The financial trends and comparisons presented below do not consider the impact that factors such as policy decisions, actual programs and services, inflation, and other elements have had on revenues.

Provincial source revenue was $1.9 billion higher than budget

2.32 In 2022-23, the Province budgeted $8.8 billion from provincial source revenue. However, actual provincial source revenue was $10.7 billion, $1.9 billion higher than budgeted.

2.33 A large portion of the nearly $2 billion in revenues over budget is attributed to adjustments from prior year estimates. PYAs are recorded as more current information becomes available. For example, the tax revenues for the year are estimated based on forecasting future economic and tax filing data since there is a delay in when the Province receives actual results (i.e., once personal tax returns are filed and assessed). Once actual filing data is received, the Province records a PYA for the difference between the original estimate and the most recent actual data. The largest PYAs are generally recorded for personal income tax, corporate income tax, and harmonized sales tax revenues. The PYAs are not budgeted; therefore, the $929 million in PYAs recognized in 2022-23 resulted in revenues being over budget and were comprised of:

- $428.6 million PYA for personal income tax;
- $288.8 million PYA for corporate income tax; and

- $212.1 million PYA for harmonized sales tax

2.34 Four of the largest provincial revenue sources in 2022-23 were:

- Personal income tax revenue $3.6 billion
- Harmonized sales tax revenue $2.4 billion
- Corporate income tax revenue $729 million
- Income from government business enterprises $465 million

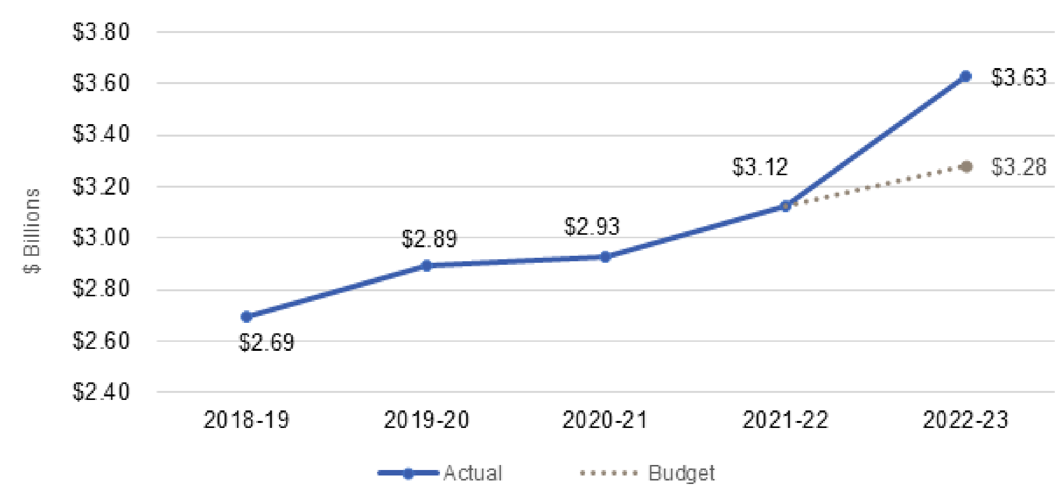
Management indicated that these PYAs reflected the high degree of uncertainty and volatility associated with COVID-19.

Personal income tax revenue was higher than both the budget and prior year amounts

2.35 Personal income tax revenue of $3.6 billion was the largest source of provincial revenue reported in 2022-23; higher than both the 2022-23 budget and 2021-22 actual amounts. It was $349 million or 10.6 per cent higher than the budget, primarily due to higher projections for both taxable income and the yield rate. Consideration of yield rates is important because income tax is calculated at progressively higher tax rates for incrementally higher income. For example, yield rate and tax collected from individuals earning higher income is greater than that collected from individuals with lower income. Higher-income individuals pay a higher tax rate on their higher levels of income and therefore the tax yield on their income overall is greater.

2.36 Personal income tax revenue has risen by close to $940 million or 35 per cent since 2018-19.

Personal Income Tax Revenue – 2018-19 to 2022-23 ($ Billions)



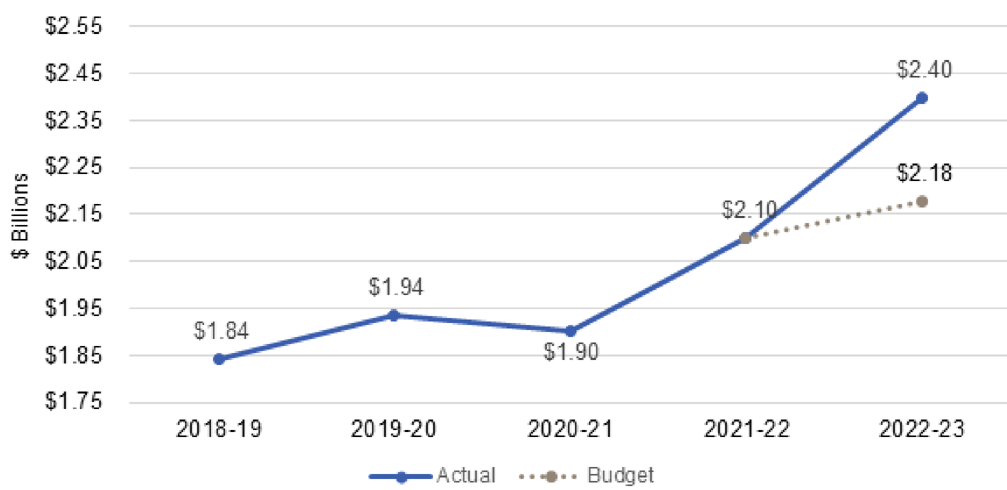
Source: Public Accounts 2019-20 to 2022-23

Harmonized sales tax revenue was higher than both the budget and the prior year amounts

2.37 Harmonized sales tax revenue was $221 million higher in 2022-23 compared to the budget, primarily due to greater residential housing investment and consumer expenditures.

2.38 Harmonized sales tax revenue has been on an upward trend since 2018-19 and has grown by $554 million or 30 per cent since 2018-19 to $2.4 billion in 2022-23.

Harmonized Sales Tax Revenue – 2018-19 to 2022-23 ($ Billions)

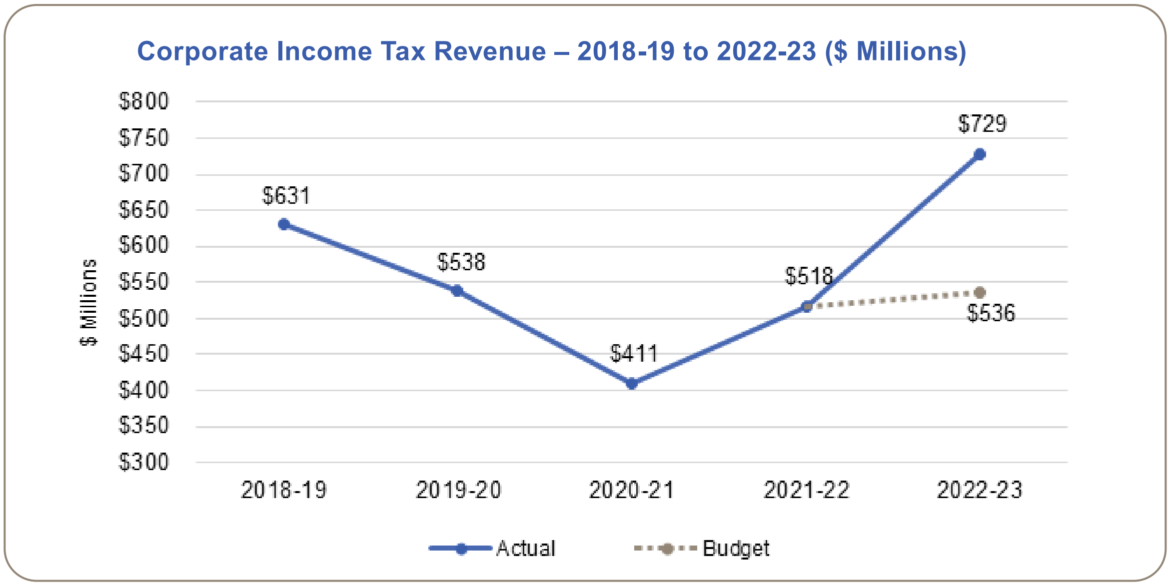


Source: Public Accounts 2019-20 to 2022-23

Corporate income tax revenue now exceeds pre-pandemic levels

2.39 Corporate income tax revenue was $193 million higher than budget in 2022-23 due to increases in the federal estimates of national taxable income even with the decline in the small business share of taxable income and a decline in Nova Scotia's share of national taxable income.

2.40 Corporate income tax revenue now exceeds pre-pandemic levels. From 2020-21 to 2022-23 there was a $318 million or 77.4 per cent increase in revenue. Over the past five years, corporate income tax revenue has increased from $631 million in 2018-19 to $729 million in 2022-23. This is a $98 million or a 16 per cent increase overall, even though the tax rate was reduced by 2 per cent to 14 per cent, effective April 1, 2020.

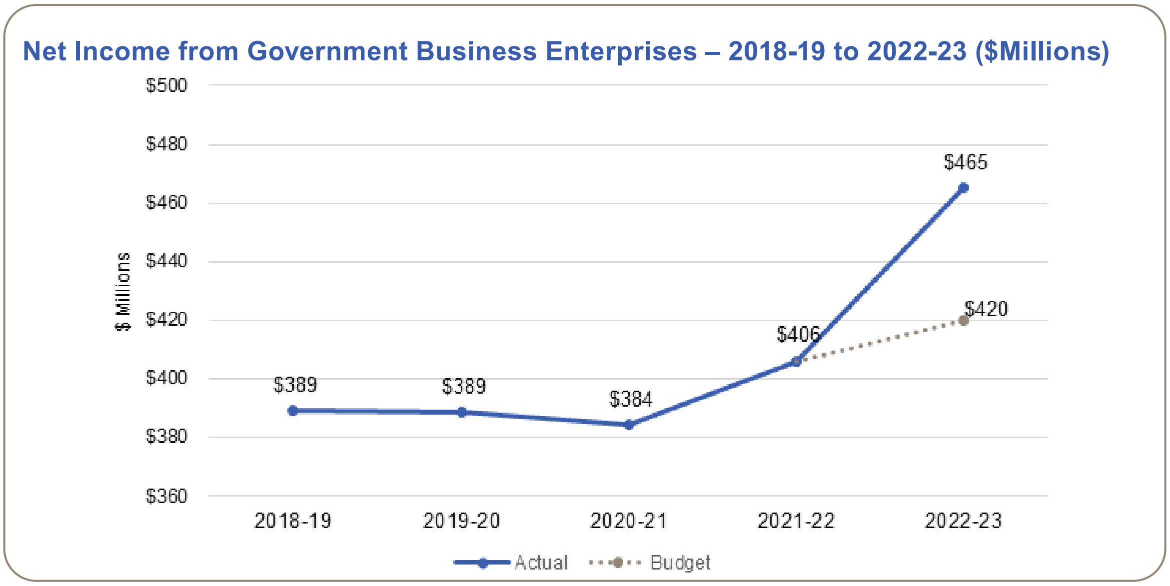


Source: Public Accounts 2019-20 to 2022-23

Net income from government business enterprises reached a peak of $465 million in 2022-23

2.41 Total net income from government business enterprises (GBEs) reached $465 million in 2022-23 and is comprised of the following:

- Net income from Nova Scotia Liquor Corporation of $285 million. This represents an increase of $16 million or 6 per cent from the prior year and is attributable to increased sales in comparison to the prior year.
- Net income from Nova Scotia Gaming Corporation of $164 million. This is $34 million or 26 per cent higher than the prior year primarily due to launch of the online casino and casino revenue returning to pre-pandemic levels.
- Net income from Halifax-Dartmouth Bridge Commission of $11.5 million. This is a $6 million or 108.4 per cent increase over the prior year and is due to increased toll revenue.
- Net income from Highway 104 Western Alignment Corporation of $5.4 million. This represents an increase of $3.4 million or 174.8 per cent, which is primarily due to a decrease in debt servicing costs and an increase in interest income.



Source: Public Accounts 2019-20 to 2022-23

Net income from government business enterprises rose $76 million or 19.5% since 2018-19

2.42 Since 2018-19, net income from GBEs has increased by $76 million or 19.5 per cent. This increase is attributable to the Nova Scotia Liquor Corporation and the Nova Scotia Gaming Corporation each reporting five-year increases of $47 million and $34 million, respectively. Other GBEs had less significant changes since 2018-19.