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Deficit-financed tax cuts amidst elevated uncertainty

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Highlights

Nova Scotia is a little over a month away from registering its eighth budget surplus in the last nine years as long as current estimates hold up. Indeed, the deficit that the province had been guiding towards ($467 million in Budget 2024 and $247 million in December's Q2 update) was erased, thanks to significant prior year provincial tax adjustments and firmer provincially sourced 2024-25 tax revenue. However, the surplus streak is likely to come to an end in 2025-26 as sales and business tax cuts usher in red ink. Specifically, the province plans to register a ~$700 million deficit in 2025-26 (1.1% of GDP, before a $200 million contingency) with the shortfall shrinking in each of the following three years. By 2028-29, the budget is expected to be balanced if the $200 million contingency is left untouched. When it comes to debt, Nova Scotia is carrying a lighter load than previously anticipated ($19.8 billion in 2024-25, equivalent to 31.6% of GDP). However, as we're seeing on the income statement, there will be balance sheet pressures in the years ahead too. The debt burden is expected to steadily rise throughout the forecast horizon, hitting 39.8% of GDP in 2028-29 (before contingencies) and surpassing the cyclical peak set at the height of the pandemic in 2020-21 (<37%). Debt servicing costs will grow at a heady clip (9.5%/year) over the coming years with the 'interest bite' expected to hit 6.8% by 2028-29. Naturally, borrowing needs are moving up too so expect to see Nova Scotia more active in debt capital markets in coming years. The $2.5 billion of long-term funding completed in this outgoing year will grow to $3.0 billion in 2025-26, $3.5 billion in 2026-27 and $3.7 billion in 2027-28 (all before contingencies).

- **Economic outlook** — After experiencing stronger growth than the country as a whole in 2023, it is estimated in the Budget that Nova Scotia's real GDP repeated this feat in 2024 with growth of 1.9% (vs. 1.3% Canada-wide). It is estimated that nominal GDP, for its part, has grown by 4.8%, also above what was registered nationally. After experiencing record growth in 2023, Nova Scotia's working-age population grew at a slower, but still impressive rate of 2.1% from January 2024 to January 2025. This strong population growth resulted in the creation of 7.8K jobs (growth of 1.5%). Nova Scotia is an exception among the Canadian provinces, as it is one of only two provinces (with New Brunswick) where the unemployment rate has not deteriorated since last year. Looking ahead, the Budget is based on real GDP growth of 2.0% in 2025, which is higher than the 1.6% expected by the average of the private sector economists. Real GDP growth should slow down to 1.8% in 2026 (still above the average private sector forecast of 1.5%) and should continue to moderate in the following years, falling to 1.5% in 2027 and 1.3% in 2028. More important for public finances, Nova Scotia's nominal GDP in 2025 is expected to grow by 4.7%, which seems somewhat optimistic compared to the private sector's forecast of 3.4%. Nominal GDP should then rise by 4.3% in 2026 (above the 3.2% expected by the consensus), 3.6% in 2027 and 3.0% in 2028. As for the labour market, job creation is expected to be slower than population growth in the coming years, consistent with the unemployment rate rising from an average of 6.5% in 2024 to 6.7% in 2025 and 6.8% in 2026.
- **Latest (but not yet final) estimate of the 2024-25 budget balance** – Today, we learned that Nova Scotia is likely to end the year with a modest surplus of $82.4 million (or 0.1% of GDP). Should this surplus hold, it will be the eighth year in the past nine that the province has ended the fiscal year in the green. This trend would extend back to FY 2016-17, with the only exception being the 'peak COVID' 2020-21 fiscal year. The fiscal results are an improvement relative to prior guidance as last year's budget foresaw a $467 million shortfall and the more recent Q2 update guided towards a $247 million deficit. The budgetary beat is a product of revenue coming in more than 6% above last year's guidance (and +2% vs. the Q2 update). That's thanks to provincially sourced receipts, including a more than $500 million upward adjustment to prior years' tax revenues. Spending was also up relative to Budget 2024 but the 2.6% overshoot was more modest than upside revenues.
- **Medium-term fiscal outlook (2025-26 & beyond)** – The surplus streak (aside from 2020-21's COVID speedbump) is set to come to an end in the fiscal year 2025-26, as the province has pencilled in a $697 million deficit (1.1% of GDP). The fiscal deterioration is the result of a forecasted 3.7% advance in spending, accompanied by a 1.8% decline in revenue. The budget highlights that expense growth has been primarily driven by departmental cost increases (up 6.2% vs. 2024-25 estimate) while the revenue decline is the result of tax cuts. It is important to note that this deficit is before a $200 million contingency, which has been put in place throughout the forecast horizon. That's appropriate given the 'very high degree' of global economic uncertainty and tariffs the province cites in its budgetary introduction. Before contingencies, Nova Scotia projects three years of improving budgetary results beginning in 2026-27, capped off by a modest ($9 million) surplus in 2028-29. Accounting for the $200 million annual contingency leaves the province with a $191 million deficit in the budget's outermost year.
- **New initiatives** - Dubbed 'Unlocking Our Potential', Budget 2025 focuses on three key elements: 'Making Life More Affordable', 'Laying the Groundwork', and 'Building a Healthy Population'. In the first section, the most noteworthy measure sees over $500M in foregone tax revenues, aimed at making life more affordable to Nova Scotians. This measure includes reducing HST by 1 per cent (to 14%) starting on April 1st, increasing the basic personal amount, and implementing the first year of inflation-indexing tax brackets, beginning January 1st. In all, these tax measures are expected to save an average family in the province more than $1,000 this year. Other efforts to enhance affordability include an increase in the minimum wage by $1.30 to $16.50, the removal of commuter tolls from two key Halifax bridges ($39M hit to revenue), and a $61.3M increase in spending to expand the school lunch program. 'Laying the Groundwork' explores allocations to build/renovate schools ($210M), expand the green economy ($35M), and support local industries in the form of creating jobs in skilled trades ($49.5M), to name some notable measures. The

final axis of the 2025 budget, 'Building a Healthy Population', announces an 8% increase in health spending relative to the prior fiscal year, with a price tag nearing $6 billion. This includes roughly $1.4 billion for various capital costs and hospital expansions, with $27M allocated to a shingles immunization program, and $19 million budgeted for the removal of hospital parking fees. Lastly, $500+ million will be allocated to help improve highway infrastructure. In all, the Capital Plan will invest $2.35 billion in projects aimed at supporting jobs across Nova Scotia.

- **Debt burden** — Nova Scotia's net debt looks to end 2024-25 at $19.8 billion, equivalent to 31.6% of GDP. That's a full 3%-pts lower than had been flagged in last year's budget. The improvement can be partially attributed to a smaller-than-planned level of debt but a 7% upside surprise on nominal GDP is doing more of the heavy lifting here. In any event, the province's balance sheet is in better shape heading into 2025-26. Starting with this coming fiscal year, the province's debt load is pointed higher. The biggest jump will come in the upcoming fiscal year as $2.7 billion of net new debt is expected to accumulate (before a $200 million contingency). That would bring the debt burden to 34.3% of GDP (or 34.6% if the contingency is utilized). The pace of debt growth will technically slow in the outer years but we're still looking at an average of $2.2 billion net new debt each year and a debt burden of 39.8% by the end of 2028-29. (Again, the utilization of contingencies would be consistent with more debt, the debt burden reaching 40.9% in this scenario). This planned accumulation leaves the level of net debt much higher than telegraphed in Budget 2024, but because of stronger GDP, the path of the debt burden ends up looking pretty similar. Indeed, the 38.4% net debt ratio projected in 2027-28 (before contingencies) is unchanged from last year's budget.

- **Interest bite** — Debt servicing costs are anticipated to grow at an average annual rate of 9½% over the coming four fiscal years, consuming a gradually larger share of provincial revenue. Nova Scotia's 'interest bite' - forecast at 5.2% in this outgoing fiscal year - is seen rising to 5.5% in 2025-26 and 6.8% by 2028-29. Note that the province has no net FX exposure on its outstanding debt, with official sensitivity analysis suggesting a 1% increase/(decrease) in T-bill yields adds/(subtracts) $10.4 million in annual interest. (For reference, debt-servicing costs are projected at $909 million for the coming fiscal year).

- **Borrowing requirement** — Nova Scotia tapped debt capital markets for $2.5 billion in 2024-25, slightly below the level of gross long-term funding outlined in Budget 2024 ($2.6 billion). Completed issuance was placed exclusively in the domestic market, the province steering fixed-rate deals to 10s and 30s while issuing a new $300 million 50-year MTN. A 7-year CORRA FRN was also part of the financing mix. In light of the expected deficits, capital spending plans and Crown Corp. advances outlined in the budget, investors can expect Nova Scotia to be somewhat more active in the coming fiscal years. For 2025-26, the budget details a total funding requirement (all sources) of $3.7 billion. With $750 million to be sourced from short-term markets or via a drawdown of short-term assets, 2025-26's gross long-term borrowing requirement amounts to just under $3.0 billion before contingencies (or $3.2 billion after contingencies). The coming year's bond crop looks once again to be steered primarily to the domestic (i.e., CAD) bond market, although documentation remains in place to access international markets. Indicatively, Nova Scotia's long-term requirement is set to increase further in 2026-27 ($3.5 billion, before contingency) and again in 2027-28 ($3.9 billion, before contingency).

- **Current long-term credit ratings** — S&P: AA-, Stable | Moody's: Aa2, Stable | DBRS: A(High), Stable
  *[Refer to our **Provincial Ratings Snapshot** for additional colour on specific credit rating drivers/considerations]*

Nova Scotia

$ Million	Budget 2024-25	Estimate 2024-25	Budget 2025-26	Estimate 2026-27	Estimate 2027-28	Estimate 2028-29
Revenues	**15,843.8**	**16,811.1**	**16,505.6**	**17,265.0**	**17,933.9**	**18,368.9**
Provincial Taxation, Fees and Charges	8,021.4	9,026.6	8,593.6			
Interest Revenues and Sinking Funds Earnings	162.8	212.6	215.4			
Federal sources	6,041.6	5,889.5	6,161.2			
Ordinary Recoveries	1,144.0	1,195.5	1,070.0	1,098.4	1,032.0	958.0
Sub-total	**15,369.9**	**16,324.2**	**16,040.2**	**16,796.5**	**17,455.6**	**17,879.3**
Net Income from Government Business Enterprises	473.9	486.9	465.4	468.5	478.3	489.6
Expenses	**16,518.7**	**16,949.5**	**17,568.7**	**18,148.2**	**18,394.9**	**18,713.4**
Departmental expenses	15,536.4	15,907.4	16,495.2	16,925.7	17,053.4	17,238.3
Refundable tax credits	126.3	153.2	148.0	162.7	162.7	162.8
Pension Valuation Adjustment	33.1	19.7	17.1	30.4	41.9	63.7
Debt Servicing Costs	822.9	869.3	908.5	1,029.4	1,136.9	1,248.6
Consolidation and Accounting Adjustments	207.5	220.9	365.6	360.6	353.1	353.1
Provincial Surplus (Deficit)	**(467.4)**	**82.4**	**(697.5)**	**(522.6)**	**(107.9)**	**8.6**
Contingency	-	-	(200.0)	(200.0)	(200.0)	(200.0)
Provincial Surplus (Deficit) - after Contingency	**(467.4)**	**82.4**	**(897.5)**	**(722.6)**	**(307.9)**	**(191.4)**
Term debt borrowing						
Provincial Deficit (Surplus)	467.4	(82.4)	697.5	522.6	107.9	(8.6)
Tangible capital assets: Net cash	1,048.1	1,316.0	1,672.0	2,039.0	2,075.0	1,860.0
Other Non-Budgetary transactions	(77.2)	(532.9)	(478.7)	(96.6)	(109.8)	111.5
Other Net Allocations to Various Funds	300.7	971.7	238.5	1,009.3	647.7	399.2
Cash Debt Retirement	859.2	859.2	841.2	3.5	1,203.4	1,103.6
Sub-total: Total borrowing requirements	**2,598.2**	**2,531.6**	**2,970.5**	**3,477.8**	**3,924.2**	**3,465.7**
Change in Short-Term Borrowing (inc)/dec	(750.0)	276.7	(750.0)	-	-	-
Total	**3,348.2**	**2,254.9**	**3,720.5**	**3,477.8**	**3,924.2**	**3,465.7**
Net Direct Debt						
Opening Balance	18,701.7	18,516.2	19,749.8	22,419.7	24,981.6	27,164.9
Provincial Balance	467.4	(82.4)	697.5	522.6	107.9	(8.6)
Increase in net book value of tangible capital assets, other	1,048.1	1,316.0	1,672.4	2,039.3	2,075.4	1,860.2
Other	-	-	300.0	-	-	-
Closing Balance	**20,217.2**	**19,749.8**	**22,419.7**	**24,981.6**	**27,164.9**	**29,016.5**
Nominal GDP	58,375	62,447	65,389	68,200	70,686	72,817
Net position: Surplus (Deficit) / GDP	**-0.8%**	**0.1%**	**-1.1%**	**-0.8%**	**-0.2%**	**0.0%**
Net Direct Debt / GDP	**34.6%**	**31.6%**	**34.3%**	**36.6%**	**38.4%**	**39.8%**
Gross Debt Servicing / Total revenues	**5.2%**	**5.2%**	**5.5%**	**6.0%**	**6.3%**	**6.8%**

Source: Budget Documents, Nova Scotia Department of Finance.

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