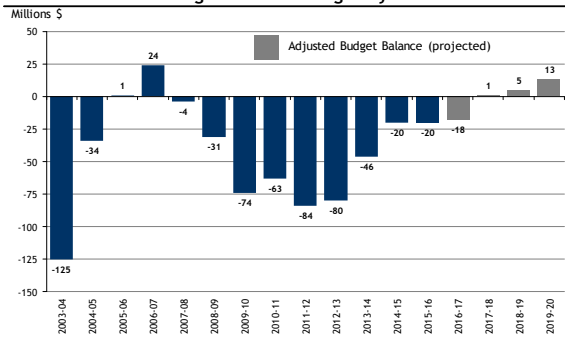


PRINCE EDWARD ISLAND BUDGET 2017

April 11, 2017

Prince Edward Island government budgetary balance



Source: RBC Economics Research, Prince Edward Island Department of Finance

Table 1: Economic Assumptions

| Year-over-year % change | Forecast | |
|-------------------------|----------|------|
| | 2017 | 2018 |
| 2017 Budget | | |
| Real GDP growth | 1.3 | 1.2 |
| Nominal GDP growth* | 3.5 | 3.5 |
| RBC Economics | | |
| Real GDP growth | 1.0 | 1.0 |
| Nominal GDP growth | 2.0 | 3.1 |

*Fiscal year basis

Source: RBC Economics, Prince Edward Island Department of Finance

Prince Edward Island returns to budget balance

After 10 years of deficits, Prince Edward Island is projecting a surplus this year making good on a long-standing government promise. Budget 2017 — introduced on April 7 — anticipates a razor thin surplus of only \$600,000 following an upwardly revised deficit for 2016-17 in which unexpected increases in expenditures and a \$30mm payment to the federal government increased the shortfall from to \$18mm. While the province is on the cusp of a return to budget surpluses, the province will continue to accumulate debt until 2020 as it funds increases in infrastructure investment.

Revenues and taxes

Budget 2017 is premised on stronger economic growth in 2017 and 2018, especially in nominal terms, which translates into a 4.6% increase in projected revenues. While the budget includes no new tax measures, last year's one percentage point increase in the provincial portion of the HST and strong income gains are expected to deliver a 6.4% increase in the tax take. While the budget gives some of this back with a 2% increase in the basic personal amount, three-quarters of the expected revenue increase is being spent on government programs. The budget did not offer concrete plans for a carbon pricing system, but pledged to include one as part of the climate change action plan to satisfy federal requirements.

Spending

Budget 2017 lays out a host of new spending measures concentrated on health care, education, family and human services, transportation and infrastructure. These new initiatives follow on unexpected cost overruns last year which have pushed overall program spending up 5.8% this year relative to last year's budget. After concluding an agreement with the Federal government for the health transfer, Health PEI is receiving new money for mental health, senior services, and staffing. New education initiatives include improving support services in schools including the hiring of nurses and therapists. The budget also gives a shot in the arm for the province's infrastructure with an expanded capital budget much of which is allocated to wastewater projects.

Borrowing and net debt

Despite the anticipated surplus, an increased pace of infrastructure investment will require \$59mm in new short term borrowing for 2017-18. The province's total net debt will continue to rise modestly peaking at \$2.2bn in 2018-19. As a share of GDP, the province's debt burden is enviable. Currently sitting at 34.5%, PEI's net debt as a share of GDP is the lowest east of Manitoba and is scheduled to decline steadily through the forecast horizon.

Commentary

After several years where unforeseen events delayed a return to budget balance, Prince Edward Island is now projecting a narrow surplus. While un-

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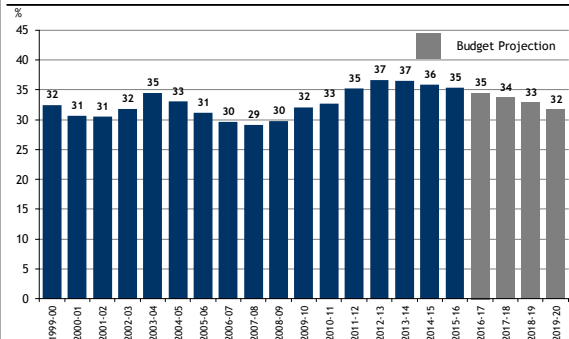
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foreseen events may yet derail the surplus given how slim it is and the lack of a contingency reserve, the province's fiscal situation is quite solid overall. After budgetary overruns in a number of departments last year, the government now has the fiscal capacity to increase spending modestly and close the deficit at once. One potential cloud on the horizon is the budget's relatively optimistic outlook for economic growth, especially on a nominal basis. Should economic growth come in slower than expected, lower government revenues may further postpone fiscal balance.

Prince Edward Island net debt-to-GDP ratio



Source: RBC Economics Research, Prince Edward Island Department of Finance

Table 2: Budget Summary (millions of dollars)

| | Forecast | | Estimate | Plan |
|-----------------------------------|--------------|------------|------------|-------------|
| | 2016-17 | 2017-18 | 2018-19 | 2019-20 |
| Total Revenues | 1,732 | 1,812 | 1,860 | 1,913 |
| Program Expenses | 1,555 | 1,614 | 1,655 | 1,699 |
| Interest | 124 | 126 | 128 | 129 |
| Amortization | 71 | 72 | 72 | 72 |
| Total Expenses | 1,750 | 1,812 | 1,855 | 1,900 |
| Adjusted Budgetary Balance | -17.9 | 0.6 | 5.4 | 12.9 |
| Net Debt | 2,196 | 2,220 | 2,239 | 2,232 |
| Net Debt to GDP Ratio | 35% | 34% | 33% | 32% |

Source: Prince Edward Island Department of Finance

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