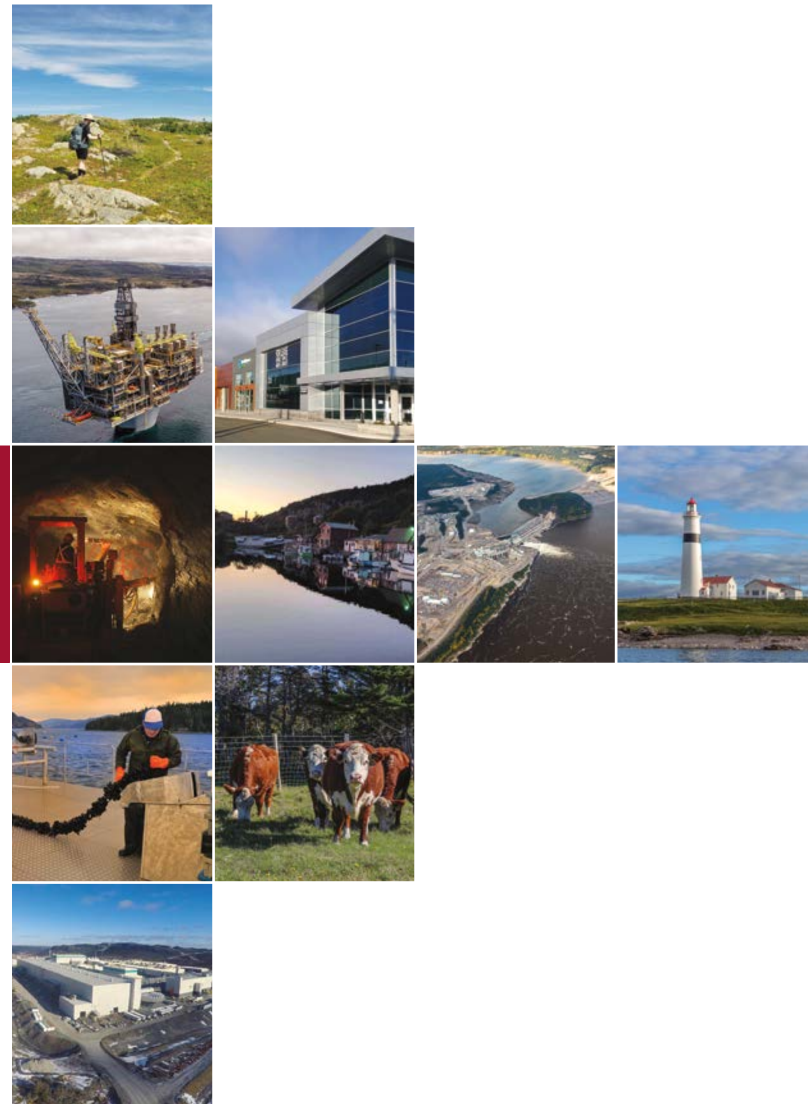
2017 Fiscal and Economic Update



Newfoundland Labrador

Fiscal Update

Budget 2017 forecast a deficit of $777.6 million. This has been adjusted to $852.4 million, primarily as a result of lower revenues. There is also a minor reduction in expenses.

The revenue deterioration of $78.8 million is primarily due to lower than expected offshore royalties and lower personal income tax (PIT) revenue. These were partially offset by improvements in Corporate Income Tax, Mining Tax and other revenues. Oil royalties, which were forecast at budget to be $881.7 million, are now projected at $734.7 million, $147.0 million lower, mainly due to a lower than expected oil price, a higher US/Canada exchange rate, and prior period adjustments. This is partially offset by higher than anticipated production. The decrease in PIT revenues is mostly due to an overestimate of the 2016 tax base data received from the Federal government.

Expenses are generally on target with Budget 2017 projections. Total expenses are expected to be $4.0 million lower than projected at budget. Expenses for government departments are projected to be $22.3 million lower than forecast at budget. This is partially offset by a projected increase in expenses by agencies, boards and commissions of $18.3 million.

The Provincial Government remains committed to returning to fiscal balance, with a focus on improving public sector efficiency and strengthening the province's economic foundation. In order to overcome the significant economic barriers to achieving this goal, government will continue to take a balanced approach, with a focus on delivering programs and services that are important to the public in a smarter and more efficient way. Government will make changes as necessary to address the ever-evolving economic and fiscal realities faced by the Province.

Statement of Operations 2017-18

	2017-18 Budget	2017-18 Fall	Variance
Revenue			
Provincial and Federal Revenue	6,897.9	6,769.4	(128.5)
Net Income of Government Business Enterprises	441.0	490.7	49.7
Total Revenue	**7,338.9**	**7,260.1**	**(78.8)**
Expenses:			
Core Government	3,808.9	3,786.6	(22.3)
Agencies, Boards and Commissions	4,307.6	4,325.9	18.3
Total Expenses	**8,116.5**	**8,112.5**	**(4.0)**
Deficit	**(777.6)**	**(852.4)**	**(74.8)**

Borrowing Requirement

2017-18 borrowing requirements have increased by $300 million from $400 million to $700 million. This is due primarily to a decrease in cash revenue of $92 million for the reasons noted above and an increase in Nalcor Energy investment of $137 million, due to the June 2017 cost increase.

Net Debt

Net debt as of March 31, 2018 is now projected to be $14.7 billion versus $15.2 billion at Budget.

Economic Update

Real GDP is expected to decline by 3.2% in 2017. While GDP is still expected to decline, this is a 0.6 percentage point improvement compared to the 2017 budget forecast. The improvement is primarily due to an increase in expected oil production for 2017.

The decrease in real GDP in 2017 stems from a decline in capital investment as construction of the Hebron oil project and the Long Harbour nickel processing facility are nearly complete. Real consumer and government spending are also expected to decline slightly this year. As a result, real final domestic demand is forecast to fall by 4.6%. Real exports are expected to increase slightly due primarily to an increase in exports of iron ore and refined petroleum.

Labour market indicators for 2017 are now expected to be weaker than forecast at budget. Employment is expected to decline by 4.1%, 2.2 percentage points lower than forecast at budget and the unemployment rate is expected to be 15.1%, 1.2 percentage points higher than earlier projected. Current expectations for labour market indicators are based on January to September data from Statistics Canada's Labour Force Survey. The decline in employment and subsequent increase in the unemployment rate in 2017 are mainly attributed to a decline in jobs related to the development of Hebron and the Long Harbour nickel plant.

Other important economic indicators, such as income and retail sales, are forecast to post stronger growth than predicted at budget. Household income is expected to increase by 1.8% this year and retail sales are expected to rise by 1.0%.

Preliminary estimates indicate that the population of the province stood at 528,817 as of July 1, 2017. This represents a decline of 0.3% compared to July 1, 2016, similar to the expectation at budget time.

Economic Indicators Forecast (Calendar Year)
Budget vs Fall 2017(per cent change unless otherwise indicated)

	2017 Budget	2017 Fall	Variance (pp*)
Real GDP	-3.8	-3.2	0.6
Household Income	-0.3	1.8	2.1
Retail Sales	-0.2	1.0	1.2
Consumer Price Index	2.9	2.6	-0.3
Housing Starts	-3.4	-17.1	-13.7
Capital Investment	-7.8	-10.6	-2.8
Population	-0.5	-0.3	0.2
Employment	-1.9	-4.1	-2.2
Unemployment Rate (%)	13.9	15.1	1.2
Participation Rate (%)	60.0	59.3	-0.7

* pp - percentage point change

Outlook

Economic growth is expected to continue to be challenged for several years beyond 2017 as further declines in capital investment are incurred and real provincial government expenditures are constrained.

In 2018 and 2019, real GDP growth is forecast to be slightly positive, as oil production from Hebron boosts total oil output. However, employment is expected to continue to decline as jobs on major project development (mainly Hebron and Muskrat Falls) decrease. Lower employment levels are expected to constrain consumption and housing starts, and contribute to a decline in the province's population.

Despite the negative outlook in the short-to-medium-term, a number of positive developments are occurring in the provincial economy. Both the Hebron oil project and the Long Harbour nickel processing plant will add to the long-term productive capacity of the economy. Total oil production is expected to increase annually for the next several years because of production from Hebron, and output from the nickel processing facility will significantly increase manufacturing shipments. Husky Energy announced that it is moving forward with development of the West White Rose project, with construction beginning this year. The construction industry is also benefitting from the provincial government's infrastructure program, which will see nearly $3 billion invested in new and existing schools, hospitals, long-term care facilities, highways and major roads, and municipal infrastructure. This program is expected to generate an average of 4,900 person years of employment per year over the next five years. There is significant interest in development opportunities in the aquaculture industry, which has the potential to double production and expand the industry into new areas of the province. To help facilitate further development, provincial government efforts are underway to increase the water area available for aquaculture, which will enable the industry to have the potential to expand commercial salmon production to 50,000 metric tonnes and commercial mussel production to 10,750 tonnes.

Diversification of the provincial economy has been identified as a priority for the provincial government. Recent actions taken by the provincial government to support diversification include: efforts to double food self-sufficiency through increasing agricultural activity, which could double direct farm employment; and investing in high performing businesses and working with technology companies to grow knowledge-based firms, such as a recent investment in PAL Aerospace's Force Multiplier project.

Moreover, there continues to be significant long-term potential in the provincial economy, particularly in the energy sector. There are substantial oil and gas resources available in offshore Newfoundland and Labrador, as evidenced by two recent resource assessments (one in the Flemish Pass and one in the West Orphan Basin) and land sales over the last three years show industry's confidence in the offshore potential. The recent land sale in the Jeanne d'Arc Region, though lower than those from the previous three years, is still positive as there continues to be interest in this mature area. In addition, Statoil, Husky, ExxonMobil and Nexen Energy are proposing long-term exploration programs for the Jeanne d'Arc and Flemish Pass areas. These programs could result in up to 65 exploration and delineation wells over the next 12 years—this demonstrates considerable commitment to the area. Exploration and development hold significant opportunities for future growth in oil production and, by extension, the provincial economy.