EXECUTIVE SUMMARY

Atlantic Canada's
Precarious Public Finances

by Ben Eisen, Alex Whalen, and Milagros Palacios

Canada's four Atlantic provinces—Prince Edward Island, Nova Scotia, New Brunswick, and Newfoundland & Labrador—face long-term threats to fiscal sustainability. COVID-19 and the resulting economic downturn has only added to these challenges. Further, they face several risks that could exacerbate their fiscal challenges in the years ahead and accelerate negative consequences. This study provides an overview of the fiscal challenges facing the four Atlantic provinces and identifies sources of precariousness that could put further pressure on public finances in the years ahead and undermine efforts to achieve sustainability.

We show, referencing two recent analyses, that the finances of all four Atlantic provinces are currently unsustainable. This means that, using reasonable assumptions, without changes in policy, the four provinces will see rising debt-to-GDP ratios over time. Many other provinces also face significant challenges to fiscal sustainability but there are a number of economic and demographic headwinds that make Atlantic Canada's finances more precarious than other regions in the country. By this, we mean that there are several possible sources of additional pressure on public finances that make the Atlantic region more vulnerable to fiscal shocks, and which will make it more difficult to achieve sustainability in the long run.

First, as a result of lower credit ratings stemming from concerns about solvency Canada's Atlantic provinces generally pay higher interest rates on newly issued government debt than most other provinces. This is why the current debt charges of the Atlantic provinces relative to own-source revenue are four of the five highest in the country. Debt charges are equal to 17.7% of own-source revenue in Newfoundland & Labrador, 10.3% in New Brunswick, 9.9% in Nova Scotia, and 9.5% in Prince Edward Island.

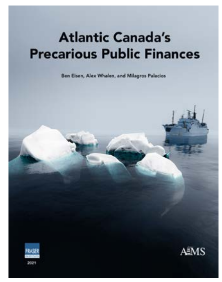
Another source of precariousness for the region's public finances are the existing high taxes in the region. These high current tax rates make it much more difficult for the province to raise taxes further at some point in the future to raise revenues to cover debt interest payments. New Brunswick has the second highest tax effort in Canada, followed by Nova Scotia in third. Prince Edward Island is fifth and Newfoundland & Labrador is sixth highest on this metric.

Another source of risk to public finances—particularly in the Maritime provinces—is the high level of dependence on transfers from the federal government. Prince Edward

Island, New Brunswick and Nova Scotia are the most reliant of any province on federal transfers to fund their programs. This is a source of vulnerability, as it means that these provinces are at greatest risk if a future federal government reduces transfer payments to the provinces.

We also show that the Atlantic provinces' demographic features will put upward pressure on health-care costs and downward pressure on labour force participation rates. Specifically, we show that the four Atlantic provinces have the four highest shares of people 65 or older in their overall population.

We conclude with an analysis of the implications of these statistics for public finances in the region. The data reveal some clues as to where the region may need to go to solve its fiscal and economic challenges. High levels of government spending relative to the size of provincial economies are a contributing factor to the region's currently unsustainable path. Reductions in spending would need to be carefully implemented but are likely a necessary ingredient for future prosperity.



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