4.1 Introduction

An important role of my Office is to provide the Members of the House of Assembly with information on the state of Government's finances. This information is necessary in order to have an informed debate about the issues that Government has to address. Issues include the ability of Government to fund programs and services, where the revenues will come from and the impact of deficits and debt.

This report provides financial and economic information to help readers understand Government's finances. The information in this report is taken from Government's Consolidated Summary Financial Statements contained in Volume I of the Public Accounts.

4.2 Key Indicators of the State of a Government's Finances

The Canadian Institute of Chartered Accountants is the professional body that recommends standards for financial reporting, accounting and auditing in the public sector. It also initiates research studies on public sector accounting and auditing matters.

The Canadian Institute of Chartered Accountants issued a Research Report in 1997 entitled Indicators of Government Financial Condition. That report identified financial indicators which it felt best describes the financial condition of a government. These indicators were categorized in terms of three elements of financial condition - sustainability, flexibility, and vulnerability.

In this report, we discuss these indicators in the Newfoundland and Labrador context. Each indicator can and should be analyzed in detail, combined with other information, and monitored over time.

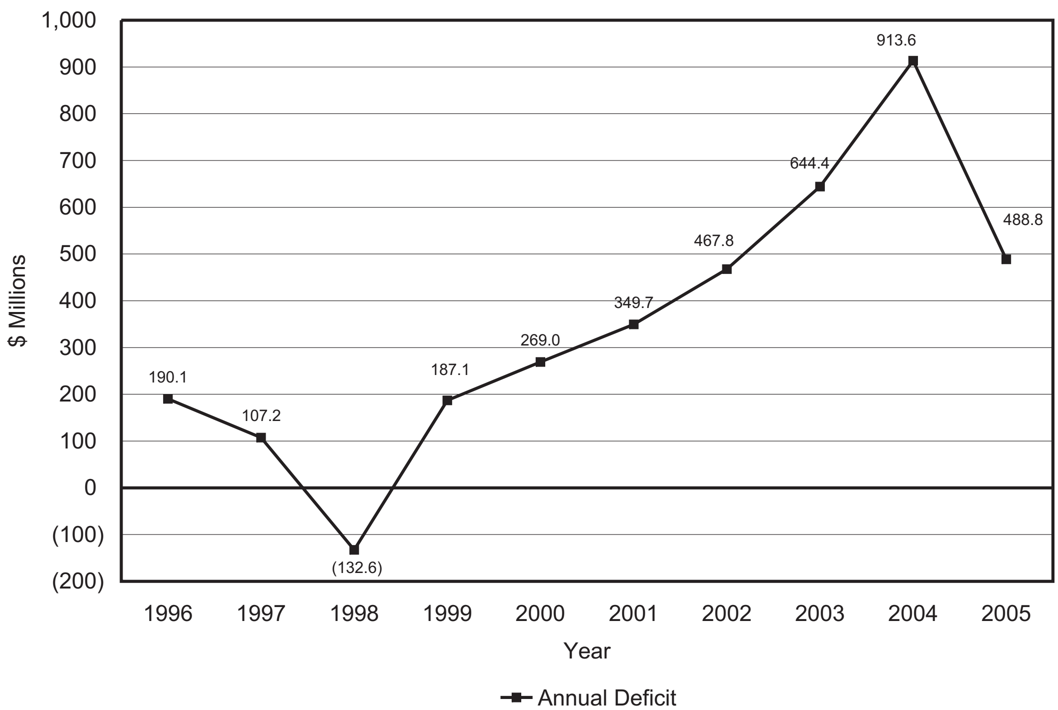
4.3 Sustainability

Sustainability is the degree to which a government can maintain existing programs and meet existing creditor requirements without increasing the debt burden on the economy. A government's annual surplus or deficit, its net debt and a province's gross domestic product (GDP) are important indicators of the state of a government's finances. Each of these indicators provides useful insight into the sustainability of a government's revenue raising and spending practices.

The annual surplus or deficit shows the extent to which a government spends less or more than it raises in revenues in one fiscal year. For the year ended 31 March 2005, the annual deficit reflected in the Province's Consolidated Summary Financial Statements was $488.8 million. Figure 1 provides details as to the annual deficit each year since 1996.

Figure 1

Consolidated Summary Financial Statements
Annual Deficit (Surplus)
Years Ended 31 March
($ Millions)



As Figure 1 shows, with the exception of 1998, Government has had an annual deficit each year. In 1998, there was a reported surplus of $132.6 million which resulted from a one-time payment of $348 million related to the Labrador ferry service transfer. The Figure also shows that Government's annual deficit grew each year from 1998 to 2004, with a peak deficit of $913.6 million in 2004, the largest annual deficit ever recorded by the Province. For 2005, Government also had an annual deficit, however, it had decreased to $488.8 million.

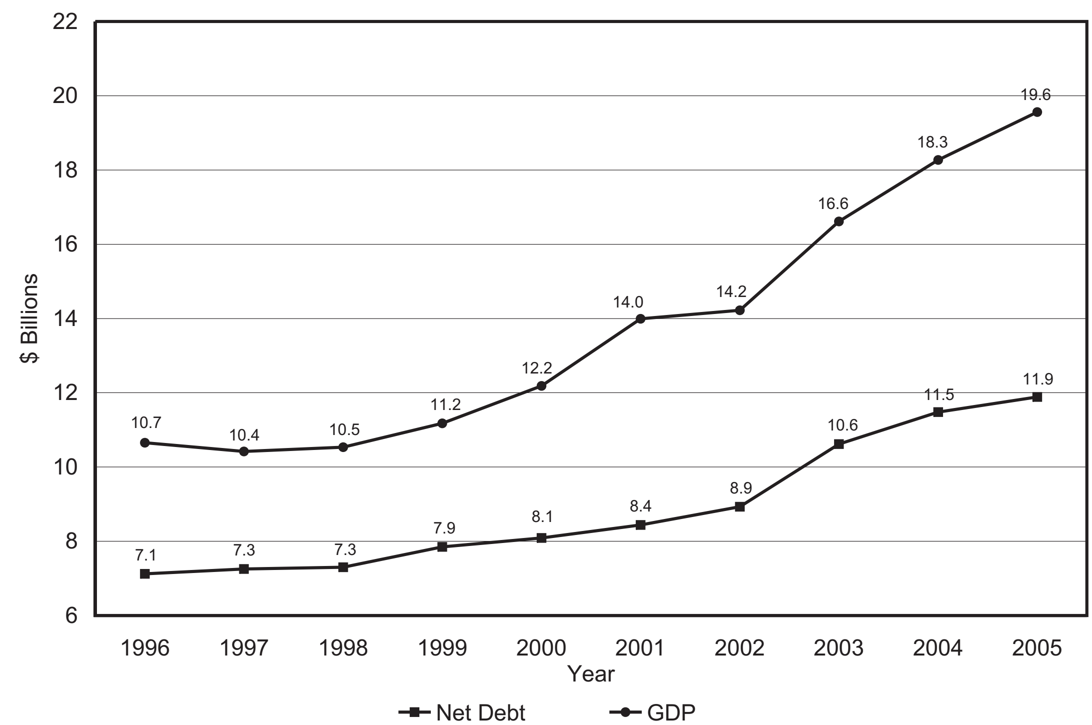
Users of a province's financial statements should look at the long-term trends such as net debt to GDP and net debt as a percentage of GDP.

The net debt is the total of all liabilities reduced by financial assets (i.e. cash and equivalents). As at 31 March 2005, the net debt reflected in the Province's Consolidated Summary Financial Statements was $11.9 billion.

The Province's GDP is a measure of the total value of all the goods and services produced in Newfoundland and Labrador in one year and indicates the size of the provincial economy. For purposes of this report we used GDP information from the Provincial Department of Finance. Government must manage its revenue raising and spending practices in the context of the economy of the Province. Figure 2 provides details as to the net debt in relation to the GDP since 1996.

Figure 2

Consolidated Summary Financial Statements
Net Debt in Relation to GDP
Years Ended 31 March
($ Billions)



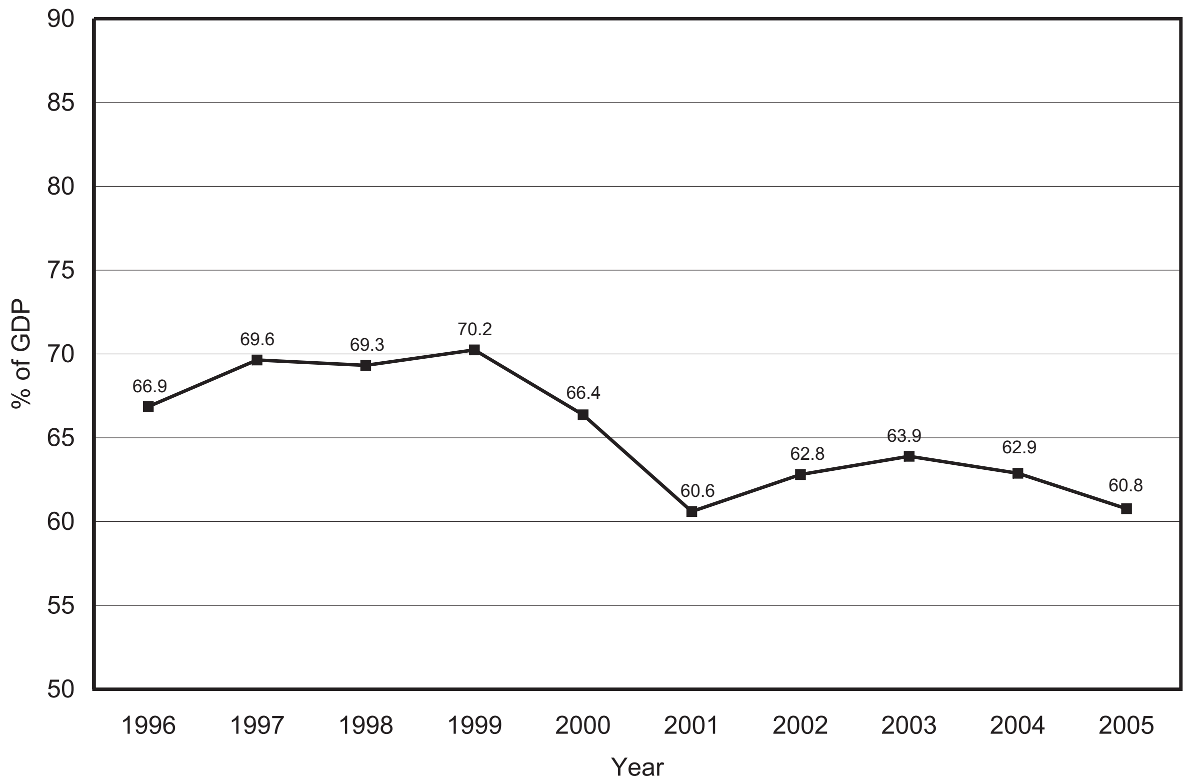
As Figure 2 shows, the GDP of Newfoundland and Labrador has increased substantially from 1996 to 2005. The 2005 GDP of $19.6 billion is an increase of $8.9 billion (83%) from the 1996 GDP of $10.7 billion. Figure 2 also shows that the Province's net debt has increased each year since 1996.

Key Indicators of the State of Government's Finances

The financial demands placed on the economy by Government's spending and revenue raising practices can be assessed for sustainability by comparing Government's net debt to the Province's GDP. Figure 3 provides a measure of how much debt Government can afford to carry. The thinking behind this measure is that the larger the GDP the more debt Government can afford to carry.

Figure 3

Consolidated Summary Financial Statements
Net Debt as a Percentage of GDP
Years Ended 31 March



The net debt of the Province as a percentage of GDP in 2005 was 60.8%, the highest net debt to GDP ratio of any province in Canada.

Government will need to carefully manage its future revenues and expenditures.