GREATER CHARLOTTETOWN AREA
CHAMBER OF COMMERCE

2010 Pre-Budget Consultations
Province of Prince Edward Island

Submitted to Honourable Wesley J. Sheridan

Minister of Finance

Introduction

The Greater Charlottetown Area Chamber of Commerce is appreciative of the opportunity to have input into the preparation of the 2010 Provincial Budget. This is important both to the Chamber and your Ministry. It forces the Chamber to focus on issues that are critical to members, while at the same time, it gives you direct information from our 900 members who employ almost 15,000 Islanders. The economic and fiscal significance of this business presence should be self-evident.

In this submission, we focus on 7 themes, all of which have critical impact on our members and their ability to create and sustain the employment base that is so important to the fiscal health of the Province:

(1) Current Economic Conditions and Trends

(2) The Provincial Government's Fiscal Performance and Future Fiscal Health

(3) Competitiveness

(4) Expenditures in Health and Education

(5) Access to Capital

(6) Follow-up to the Chamber's Business and Immigration Forums

(7) Municipal Accountability

1. Current Economic Conditions and Trends

We begin our brief with a look at economic conditions and trends, because this is the backdrop against which we offer our comments and recommendations on the other six themes.

First, a snapshot of how the PEI economy has been doing relative to Canada as a whole, and to our neighbour, Nova Scotia. The measure we have chosen is Gross Domestic Product per Capita for the period 2001 to 2008. This measure takes into consideration both changes in overall economic activity and in population. Table 1 shows that Prince Edward Island is holding its own relative to Canada and Nova Scotia. In fact, during the downturn in 2002, PEI's economic performance was better than both and the same can be expected in 2009, leading to PEI's GDP per Capita as a % of Canada's returning to the 2002 level of 73%.

Table 1			GDP per Capita		
	Canada	PEI	NS	PEI as % of Canada	PEI as % of NS
2001	$35,722	$25,106	$27,786	70.3%	90.4%
2002	$36,771	$27,039	$28,964	73.5%	93.4%
2003	$38,343	$27,678	$30,775	72.2%	89.9%
2004	$40,146	$28,931	$31,780	72.1%	91.0%
2005	$42,606	$29,669	$33,263	69.6%	89.2%
2006	$44,487	$30,808	$33,841	69.3%	91.0%
2007	$46,549	$32,506	$35,189	69.8%	92.4%
2008	$48,011	$33,159	$36,503	69.1%	90.8%

Turning to recent economic performance, the provincial and local economies appear to be weathering the recession reasonably well. The Conference Board has suggested that PEI will be one of only four provinces to show any positive increase in GDP in 2009. There are, however, significant issues buried within the results of economic performance, January to September, 2008 to 2009, as highlighted below in Table 2.

Table 2	% Change Jan. to Sept. 2008 to 2009	Total in 2008 (000)	Notes
Gross Domestic Product	N.A.	$4,624,000	
Total Manufacturing Shipments:	-5.0	$1,433,567	
Food Industry Shipments	-18.1	$883,833	Suggests a problem area
Non-food Shipments	17.0	$549,734	Very strong performance
Farm Receipts:	6.8	$390,303	
Potatoes	14.9	$200,874	Half of Total Farm Receipts
Cattle	21.6	$18,125	
Hogs	-37.4	$15,973	Industry clearly in adjustment
Dairy	6.5	$67,233	Benefits of controlled marketing
Total Exports	0.6	$848,600	
Agriculture & Fishing	-1.9	$521,100	
Industrial Goods	33.3	$18,300	Very strong performance but only a small % of total exports
Retail Sales	-1.4	$1,720,881	Perhaps positive if gasoline price changes are factored in
Total Labour Income	4.7		Strong hedge during a recession
Building Permits	-15.2	$216,946	
Residential	0.1	$118,255	
Non-residential	-32.0	$98,691	
Employment - Province	-2.0	70.2	
Employment - Ch’town	-3.3	32.9	Charlottetown area is 47% of Prov.

While overall employment levels in the provincial and local economies are down, the change is well within what should be expected, given the global and national recessions. Unemployment also has not shown dramatic increases. However, the value of building permits is down some 15%, with non-residential permits down 32%. The value of manufacturing shipments is also down (-5%), with food industries down significantly at -18%.

Of note, and perhaps of concern, is the continued and increasing negative personal savings rate as shown in Table 3. A negative personal savings rate indicates that individuals and families are using their savings, or borrowing, to maintain current consumption. As this may have significant impact on the future business environment, the Chamber requests that this matter be reviewed in detail by your Ministry, who in turn would inform the Chamber of anticipated impacts.

Table 3 Personal Savings Rate (%)

	Canada	PEI
2002	3.5	0.8
2003	2.5	-3.1
2004	3.2	-4.2
2005	2.1	-4.8
2006	3.5	-4.8
2007	2.5	-7.3
2008	3.7	-8.6

Personal Savings divided by Personal Disposable Income times 100

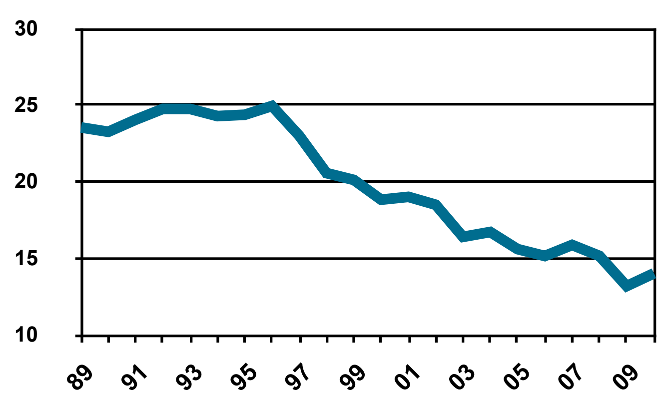
From the Chamber's perspective, since the provincial and local economies have weathered the recessionary storm quite well, it seems reasonable to expect that this should allow the Provincial Government to hold its own in terms of fiscal performance.

2. The Provincial Government's Fiscal Performance and Future Fiscal Health

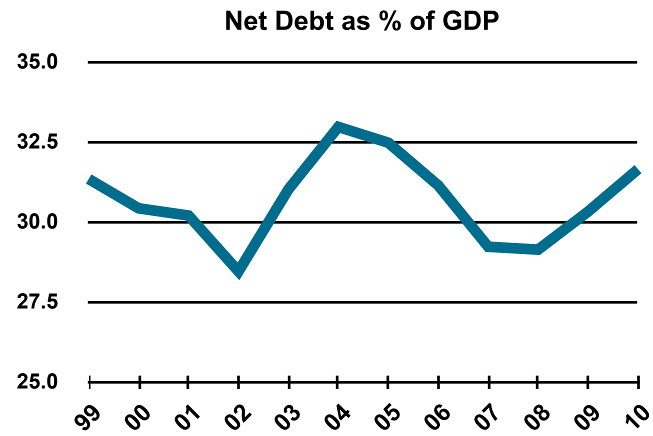
As Budgets come and go, often overlooked are trends in revenues and expenditures as well as the changing size of government relative to the overall economy. While deficit financing has been the norm over the past two decades, the following points suggest some long-term improvement in the fiscal health of the Provincial Government:

(2.1) Debt Service as a % of own-source revenues has shown significant decline, reflecting the decline in interest rates. This means that relatively more revenue has been available to fund program expenditures.

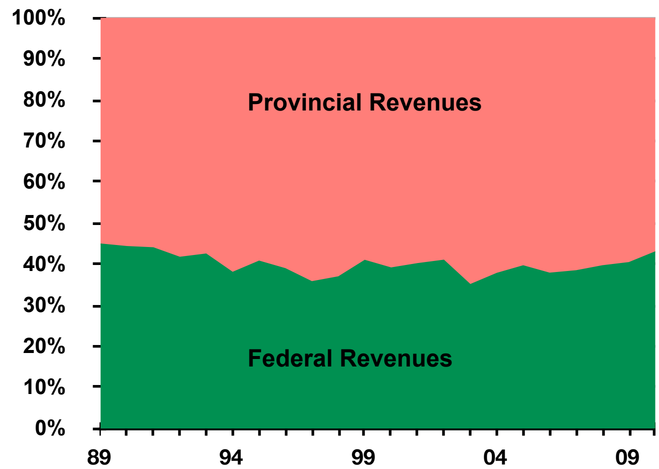
Debt Service as % of own-source revenues



(2.2) While Net Debt has continued to increase, the ratio of Net Debt to GDP over the past ten years has hovered around 30%, with a renewed upward trend in FY 2008. Thus, growth in the economy has been keeping pace with the growth in net debt.



(2.3) The breakout of federal and provincial own-source revenues shows that the Province has been able to cope with a decreasing federal share from 1989 to 2003. Since 2003, there has been an increase in the federal share, possibly reflecting an increase in federal transfers for infrastructure and labour market programs.



Nevertheless, the budgets of 2008/09 and 2009/10 are a serious cause for worry. With continued deficit financing comes higher debt service costs and a reduction in program flexibility. A strategy must be in place to deal with the current deficit, a strategy that is public and identifies what actions are planned on both the taxation and program fronts. The Province's budget is vulnerable to a number of critical factors including higher interest rates, federal pressures to keep the main statutory transfers of equalization and health in check, a reduction in discretionary federal transfers, and continued pressures for expanded health and social service programs. Without a deliberate strategy, these vulnerabilities could easily turn the fiscal situation from unfavourable to a profound challenge.

The Chamber strongly recommends that a balanced provincial budget should become the norm and not the exception. While the current recession will have a serious impact on the province's bottom line, a strategy to return to balance is required.

3. Competitiveness

The Chamber is most concerned over three competitive challenges and competitive barriers facing Island businesses: taxation; energy costs; and a shortage of labour, particularly skilled labour.

(3.1) Taxation

The Chamber has suggested in previous submissions that the provincial tax structure and tax rates are in need of review. This is even more urgent given the decisions of Ontario and British Columbia to harmonize their retail sales taxes with the GST. The evidence supporting the positive impact of harmonization on economic competitiveness is incontestable. The political ramifications of differing impacts on consumers is what has delayed implementation in provinces beyond the original four[1]. Clearly, both Ontario and British Columbia have now recognized that a strong, competitive economy will do more to raise overall consumer well-being than would continuing with separate provincial retail sales taxes.

> ***To illustrate, the marginal effective tax rate on new business investment in PEI is more than three times higher than that in New Brunswick.***
>
> ***(Data adapted from Federal Finance)***

Business confidence in PEI would benefit if the Provincial Government made it known that it supports the concept of a harmonized sales tax (if it does), and that the stumbling block is not the concept itself, but adequate compensation to offset provincial revenue losses and to protect those consumers who may be negatively affected.

(3.2) Cost of Electricity

The Chamber is very concerned over the enormous cost differential which may result from the purchase of NB Power by Hydro Quebec. Without new arrangements regarding electricity cost structures/rates, Island businesses could be paying upwards of 50% more than the competition across the Northhumberland Strait. It does not take much insight to recognize that such a differential would be almost catastrophic, particularly for large, intensive users. The Chamber is encouraged by the ‘government to government’ discussions now underway and can only hope that the result will be positive. If ever there was a case where ‘the status quo is not an option’, it would be the sale of NB Power without a significant ‘new deal’ for Prince Edward Island.

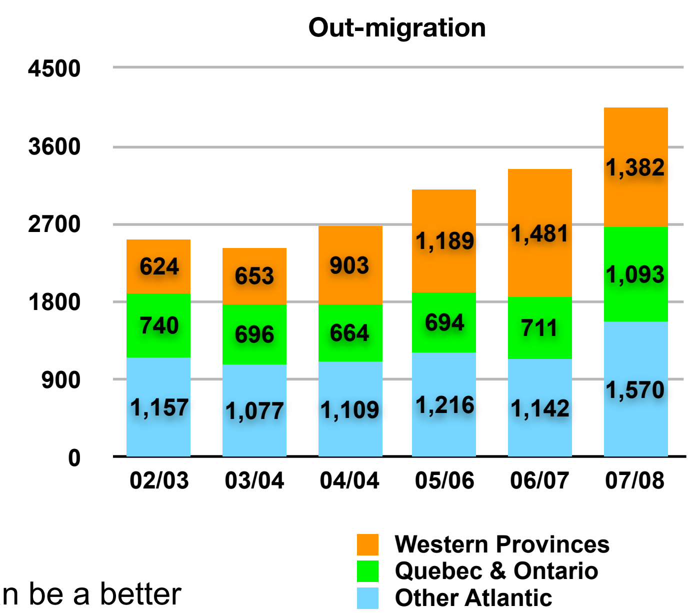
[1] Includes Quebec

(3.3) Labour Force Deficit

The recent Immigration Forum hosted by the Chamber reconfirmed a looming labour force deficit, an issue that we have included in previous submissions. With the decline in natural population increase (births minus deaths), net domestic and international immigration will be the only significant source of population and labour force growth. As the province is already experiencing labour shortages, with clear evidence that the situation is only going to get worse, the Chamber stresses that this is a critical issue and deserves the closest of attention. The province's Population Secretariat, along with a population strategy, are positive steps. But without a focus on retention, comparable in scale and effort to the current focus on attraction, the impact of the current population strategy on the labour force deficit will be marginal.

> ***Within a very few years, there will be more individuals leaving the workforce than entering it.***

The concentration on international immigrants should not take away from a focus on inter-provincial migration. Of particular concern is out-migration to other provinces of young, skilled workers. Between 02/03 and 07/08, over 18,000 individuals moved to other provinces. 40% went to other Atlantic Provinces, 25% to Quebec and Ontario, and 35% to the Western Provinces. The Chamber would welcome any analysis the Province has on who goes, and why, so there can be a better understanding of what, if anything, can be done to reverse current trends.



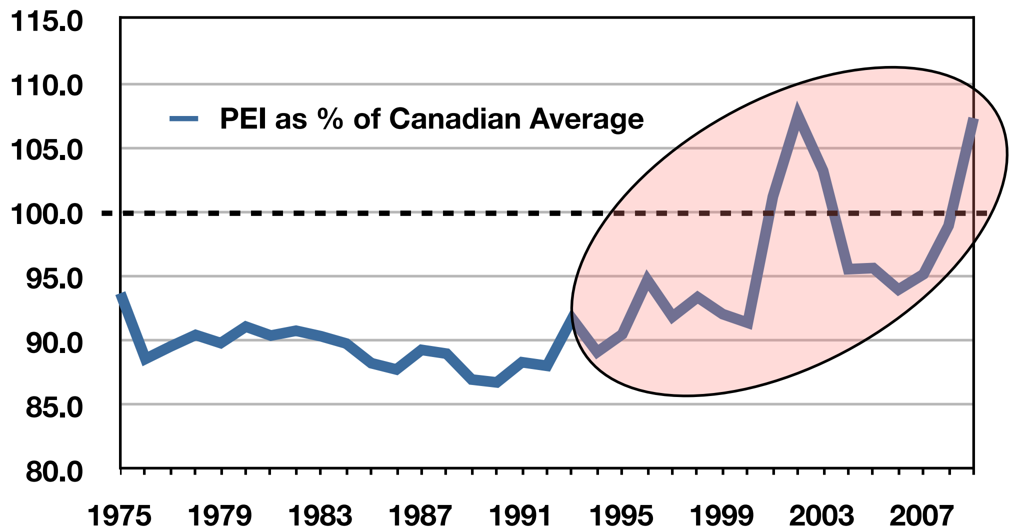
4. The Main Areas of Expenditures - Health and Education

(4.1) Health

The Chamber has concerns over both short and long term public sector health expenditures. First, some historical data. As shown in the next chart, there has been a very significant change in per capita spending on health, PEI relative to Canada.

From 1975 through to 1995, PEI's public sector Health expenditures were averaging less than 90% of the Canadian average. But over the past 15 years that trend has been decidedly upward and by 2009 PEI spending was 107% of the average of the other provinces. This is definitely not sustainable, despite apparent needs and demands.

Provincial Government Health Expenditures per Capita, PEI as % of Canada



Source: Canadian Institute for Health Information,
National Health expenditure Data Base

Without matching expenditure reductions in other program areas, continuing to spend more on health per capita than the Canadian average will place a serious financial burden on the province's finances, leading to continued deficit financing or tax increases that will stifle economic development.

The Chamber's second concern regarding health expenditures is based on demographic changes underway. As the baby boomers (and the boomer echo) age, the ratio of young and old to the working age population is expected to show dramatic change. It is well established that the population over 65 accounts for a substantial portion of health care expenditures. *"Seniors age 65 and older consumed more than 44% of all provincial/territorial government health spending in 2007, while comprising only 13.5% of the population"*. [2] When coupled with population projections showing a substantial increase in this population group over the next two decades, pressures on healthcare spending could be enormous.

[2] Canadian Institute for Health Information, National Health Expenditure Data Base, page 44.

(4.2) Education

The dynamics with regard to education are markedly different than health. As the province's birth rate fell, so did grade 1 enrollments. This trend has affected, and will continue to affect the school system for the next decade or more. The Provincial Government seems to be adapting well to these changes as reflected in per pupil expenditures.

With both health and education, the Chamber encourages continued vigilance and sound planning to adjust to known demographic change.

5. Access to Capital

Access to capital is key to business investment and job creation. Sources of capital for business development and expansion in the province appear to be adequate (PEI Business Development, Atlantic Canada Opportunities Agency, Business Development Bank, commercial banks etc.). Nevertheless, the availability of capital for businesses in an early stage of development, looking for investors to initiate product commercialization, may be wanting. This applies in particular to the sectors that the province is focusing on in its Prosperity Strategy.

The Chamber believes that a thorough examination of the demand and supply for private equity financing in the province would be beneficial, including immigrant investment, venture capital - both institutional and private (angel investors), and growth capital. In addition to demand and supply for private equity, the examination should include a comparison of tax credits available in the other Atlantic Provinces. For example, the Chamber is aware that PEI is the only Atlantic Province that does not provide a tax credit for contributions by individuals to GrowthWorks Atlantic, a Labour Sponsored Venture Capital Corporation investing in Atlantic Canada.

The Chamber offers its support and member expertise in the carrying out of an examination.

6. The Chamber's Business and Immigration Forums

During the past year, the Chamber has hosted two Forums - A Business Forum in February and an Immigration Forum in late October. Both were very successful, bringing interested parties together to share information and identify issues and opportunities. Copies of the Reports of both Forums are available from the Chamber. Following, and for your information, are the Themes of each Forum.

Themes of the Business Forum:

1. Zoning and Development Bylaw - in need of review
2. Vibrancy of the Downtown - needs a focused and coordinated effort
3. Efficiencies and value for money in City operations and finances

   "It was recommended that appropriate Provincial legislation should be amended to require external audits of City operations and finances, with public reporting of the results."

4. Cooperation and Partnerships
5. Development Tax Incentive Programs
6. Harmonized Sales Tax

   It was suggested that the GCACC, on behalf of the business community, approach the Provincial Government to initiate a review of the merits of harmonization.

7. Infrastructure - aging and in need of significant investment
8. Permanent Site for Events and Concerts - now under investigation
9. Further Development of the Waterfront (commercial and residential)

Themes of the Immigration Forum:

1. The Demographic Challenge

   ". . . clear that more can and must be done to inform the general public, municipal leaders, business leaders and labour of the absolute need, and not just the desire, to attract and retain newcomers to the province."

2. Keeping Retention in Pace with Attraction

   ". . . some urgency to incorporate specific retention strategies as an integral part of attraction and recruitment efforts."

3. Promoting a Welcoming Community
4. Enhancing Language Training

   ". . . language training resources should meet the demand generated by vigorous immigrant attraction programs."

5. Establishing Connections
6. Leadership and Coordination

7. Municipal Accountability

Chamber members have, for some time, discussed the need for better municipal accountability and transparency, with more attention to performance measurement and the public reporting of results. Business development is closely linked to the health and vibrancy of the province's municipalities, and that, in turn, is directly related to fiscal and operational management.

The Province has made significant strides in municipal financial reporting as evidenced by the standardized Municipal Financial Information Return (MFIR). It is not, however, sufficient to report on what is being spent; of equal importance is what is being delivered (service levels) and what is being achieved.

Since municipalities are creations of the Province, the Chamber recommends that the Provincial Government amend the *Municipalities Act, Charlottetown Area Municipalities Act and the City of Summerside Act* to establish the requirement that all cities and towns must report on performance, following a standardized performance reporting framework established by the Province in consultation with these municipalities. This would be a logical extension of the MFRI.

This is not a new concept. The Province of Ontario, for example, since 2001, has required its municipalities to report performance via the Municipal Performance Measurement Program.

> "Municipal performance measures are authorized under the *Municipal Act, 2001*. Every year the Minister writes to municipalities, informing them of the formal requirements of the program, including a list of performance measures. The Minister's letter and the annual list of performance measures are posted on the Ministry's web site under the heading, Municipal Performance Measurement Program."[3]

The implementation of municipal performance measures in PEI would benefit both municipalities and taxpayers; it would provide municipalities with much needed information on program efficiencies, and taxpayers with information on how service levels are changing over time, relative to changing tax contributions.

The Chamber urges consideration of this measure to improve municipal accountability.

[3] http://www.mah.gov.on.ca/AssetFactory.aspx?did=6851

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- Develop and implement a strategy to achieve and maintain a balanced budget, particularly in light of the impact on debt service from expected increases in interest rates.

- Address the following issues that affect business competitiveness:

  - Provincial Government's position re the HST
  - Impact of the pending sale of NB Hydro on electricity rates
  - Labour force deficit (skill shortages, migration)

- Give close attention to the big spending areas of health and education, given demographic changes underway, and very limited fiscal maneuverability.

- Assess access to capital, particularly private equity.

- Implement a municipal performance initiative that would bring benefits to both municipalities and taxpayers.

The Chamber thanks you for this opportunity to discuss fiscal and economic issues. The challenges ahead are many, but with the best information and the resolve to act, our "One Island Community" will be well served.

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