FISCAL AND ECONOMIC OUTLOOK

DEPARTMENT OF FINANCE
GOVERNMENT OF NUNAVUT

FEBRUARY 22, 2012

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1 Fiscal Outlook

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- **Expenditures.** The GN is budgeting to spend **$1,341.6 million** in 2012-13.
- **Surplus.** The GN forecasts a surplus of **$37.7 million** in 2012-13, after setting aside $78.5 million for contingences and subtracting $18.5 million earned by revolving funds.

Fiscal Summary

The GN expects revenues of $1,476.3 million and is budgeting to spend $1,341.6 million in 2012-13. After setting aside $78.5 million for contingencies and supplementary appropriations and subtracting $18.5 million in revenues (net cost of goods sold) from revolving funds, the GN projects a surplus of $37.7 million. This follows a projected deficit of $58.5 million in 2011-12, after adjusting for lapses and capital carryovers (Figure 1-1). This presentation differs from that used to prepare the Non-Consolidated Financial Statements (NCFS) included in the Public Accounts. For example, the NCFS also accounts for revenues and expenditures associated with third-party funding, as well as expenses such as amortization. We discuss the differences between these two presentations below.

Figure 1-1: Fiscal Performance

$ thousands	Main Estimates 2012-2013	Revised Estimates 2011-2012	Main Estimates 2011-2012
Total Revenues	1,476,324	1,366,578	1,374,478
Total Expenditures	(1,341,575)	(1,454,703)	(1,316,873)
Less: Revenues from revolving funds	(18,526)	(18,578)	(18,578)
Less: Supplementary Requirements	(78,500)	(39,000)	(89,000)
Surplus (Deficit) before lapses and carryovers	**37,723**	**(145,703)**	**(49,973)**
Plus: Lapses[1]		12,000	
Plus: Projected Capital Carryovers to next year		45,700	
Less: Projected Capital Carryovers from prior year	(45,700)		(38,400)
Accounting Surplus (Deficit)	**(7,977)**	**(88,003)**	**(86,373)**
Less: Projected Capital Carryovers to next year		(45,700)	
Plus: Projected Capital Carryovers from prior year	45,700	75,200	38,400
Surplus (Deficit) excluding capital carryovers	**37,723**	**(58,503)**	**(49,973)**

1. Includes $10 million in O&M lapses as presented in the Main Estimates' Summary of Operations and $2 million in capital lapses that are not carried over.

Revenues

The GN expects to receive $1,476.3 million through federal transfers, taxes, and own-source revenues in 2012-13. This is $109.7 million, or 8.0%, more than the $1,366.6 million we expect to have received from these sources in 2011-12. When we consider the additional $130.6 million we anticipate through third-party funding agreements in 2012-13, the projected revenues as recorded on the Public Accounts basis rise to $1,606.8 million.

Figure 1-2: Summary of Revenues

$ thousands	Main Estimates 2012-2013	Revised Estimates 2011-2012	Main Estimates 2011-2012	Actual[1] 2010-2011
Total Federal Transfers	**1,356,098**	**1,250,800**	**1,258,000**	**1,165,161**
Total Own-Source Revenues	**120,226**	**115,778**	**116,478**	**162,705**
Own-Source Taxes	71,300	66,800	63,000	70,672
Own-Source Revolving Funds (net of CoGS)	18,526	18,578	18,578	49,295
Other Own-Source	30,400	30,400	34,900	42,738
Total Revenues (Main Estimates basis)	**1,476,324**	**1,366,578**	**1,374,478**	**1,327,866**
Revenues from third-party agreements[2]	130,569	101,397	93,370	116,151
Total Revenues (Public Accounts basis)	**1,606,793**	**1,467,975**	**1,467,848**	**1,444,017**

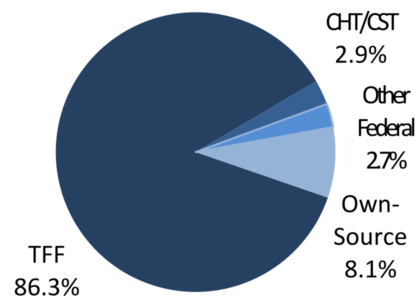
1. GN Finance generated data used to prepare the 2012-13 Main Estimates before finalizing the 2010-11 Public Accounts. Due to adjustments in the intervening period, some 2010-11 figures in the Main Estimates do not match figures in the Public Accounts. We present the final 2010-11 Public Accounts figures throughout this Fiscal Outlook.
2. The Main Estimates Summary of Operations presents third-party funding for O&M and Capital in 2012-13, but only for O&M in other columns. This Fiscal Outlook presents third-party funding for O&M and Capital for all years.

Federal Transfers

Transfers from the federal government will provide $1,356.1 million to the GN in 2012-13. The Territorial Formula Financing (TFF) arrangement is by far the largest component of GN revenues, contributing 86% of the GN's appropriated revenues on its own (Figure 1-3).

Figure 1-3: Revenue Sources

% of GN 2012-13 revenues



The Canada Health Transfer (CHT) and the Canada Social Transfer (CST) are also important transfers, but are quite small relative to the TFF, together contributing only 2.9% of revenues. The TFF, CHT and CST make up the core of the long-term, legislated fiscal relationship between the GN and the federal government. Shorter-term programs and one-time grants provide the GN with important but fluctuating sources of additional funds, contributing $40.3 million in 2012-13.

Third-Party Funding Agreements

The GN receives funding from external organizations (largely the federal government) through third-party agreements. As organizations often target these funds to support specific areas or projects, the GN considers these revenues differently from those over which the Legislative Assembly has complete spending discretion, such as unconditional federal transfers and taxes.

Due to this distinction, the GN occasionally segregates third-party funding in its calculations. For example, we do not include third-party funding when describing the GN's spending appropriations through the Main Estimates, but do report third-party funding in our Public Accounts, which record the GN's complete financial flows in a year.

The GN currently expects to receive $130.6 million through third-party agreements in 2012-13, although these agreements can be difficult to predict. Funding flows from large national programs such as the Gas Tax Fund and the Building Canada Fund as well as dozens of smaller "boutique" programs that support a wide range of initiatives. We provide a breakdown of these initiatives in Appendix IV of the 2012-13 Main and Capital Estimates. Although the GN receives third-party revenues from other sources, the substantial majority (97% in 2010-11) comes from the Government of Canada.

Figure 1-4: Revenues from the Government of Canada

$ thousands	Main Estimates 2012-2013	Revised Estimates 2011-2012	Main Estimates 2011-2012	Actual 2010-2011
Territorial Formula Financing (TFF)	**1,273,498**	**1,175,300**	**1,175,300**	**1,090,553**
Other Transfers	**82,600**	**75,500**	**82,700**	**74,608**
Canada Health Transfer (CHT)	30,832	28,994	30,035	26,814
Canada Social Transfer (CST)	11,425	11,083	11,188	10,854
Miscellaneous Federal Transfers	40,343	35,423	41,477	36,940
Revenues from Federal Transfers (Main Estimates basis)	**1,356,098**	**1,250,800**	**1,258,000**	**1,165,161**
Revenues from third-party agreements[1]	130,569	101,397	93,370	116,151
Federal	*(note)*	*(note)*	*(note)*	**112,439**
Other	*(note)*	*(note))*	*(note)*	3,712
Total Federal Revenues (Public Accounts basis)				**1,277,600**

1. *We do not distinguish third-party funding by source (federal or other) when preparing estimates, but do make this distinction in our Public Accounts.*

Own-Source Revenues

Own-source revenues flow from taxes, revolving funds and other income streams, including a number of small miscellaneous sources such as user fees, licenses or fines. The GN expects to collect $120.2 million in own-source revenues in 2012-13. This is $4.4 million greater than the previous year but is down from 2010-11, when the GN's Petroleum Products Division (PPD) received about $20 million more (net cost of goods sold) than it had projected from fuel sales. As revolving funds are intended to support specialized government operations rather than raise general revenue, the GN considers them differently from other revenue sources for annual budgeting purposes (Figure 1-5).

Revolving funds *retain funds from one fiscal year to the next to finance a continuous cycle of special government operations. Only a few revolving funds exist, including the Liquor Revolving Fund and the Petroleum Products Revolving Fund. These operate on a cost-recovery basis, and must pay back initial capitalization costs. Due to the unique nature of revolving funds, which are not intended to regularly generate general revenues, the GN occasionally segregates the associated revenues and expenses from those of other government functions.*

Figure 1-5: Own-Source Revenues

$ thousands	Main Estimates 2012-2013	Revised Estimates 2011-2012	Main Estimates 2011-2012	Actual 2010-2011
Own-Source Taxes	**71,300**	**66,800**	**63,000**	**70,672**
Personal Income Tax	18,400	17,000	17,000	19,816
Corporate Income Tax	8,400	7,500	7,500	9,034
Fuel Tax (net of Fuel Tax Rebate)	4,200	3,800	3,100	5,924
Property Tax	2,700	2,700	1,700	2,019
Tobacco Tax (net of commissions)	14,600	13,800	12,700	13,058
Payroll Tax	22,300	21,300	20,300	19,803
Insurance Taxes	700	700	700	1,018
Own-Source Revolving Funds	**18,526**	**18,578**	**18,578**	**49,295**
Liquor Commission, net of CoGS[1]	5,265	4,405	4,405	3,668
Petroleum Products Division, net of CoGS[1]	13,261	14,173	14,173	45,627
Other Own-Source	**30,400**	**30,400**	**34,900**	**42,738**
Rental Recovery – Staff Housing	15,500	15,500	15,000	16,224
Miscellaneous Revenues	14,900	14,900	19,900	15,696
Recovery of Prior Years' Expenditures	–	–	–	10,818
Total Own-Source Revenues (Main Estimates basis)	**120,226**	**115,778**	**116,478**	**162,705**
Total Own-Source Revenues (w/o revolving funds)	101,700	97,200	97,900	113,410

1. Cost of Goods Sold

Tax Revenues

The GN projects $71.3 million in tax revenues in 2012-13, about $4.5 million greater than 2011-12, and slightly more than the $70.7 million we actually received in 2010-11. We estimate that taxes on payroll and personal income alone will contribute about $40 million, more than half the total amount. Based on January 2012 estimates, we forecast tobacco tax—which rounds out the GN's largest three tax streams—will generate $14.6 million.

Looking ahead, we expect Nunavut's growing private sector will continue to increase GN revenues, particularly through payroll and personal income taxes. Eventually, there may be important gains from Nunavut's corporate income tax (CIT), but we do not expect significant jumps over the medium term. The GN raised about $9 million in CIT in 2010-11, though we have budgeted to receive slightly less in 2012-13.

Nunavut's relatively small level of corporate tax revenues has meant that it has not been crucial for the GN to be able to forecast long-term CIT income. This is changing as more mining projects advance through the regulatory process. Mining firms are important for Nunavut's economy and communities, particularly as a potential source of local employment for those with the right skills. It is not yet clear, however, how mines will impact the GN's own finances.

Canada's corporate tax laws recognize mining is different from other industries. For example, investments in mining are relatively risky: firms work for many years to explore and develop a mine without being entirely sure about what revenues they will generate. Also, mining projects often require corporations to make large capital investments up front.

Canada's tax laws provide mining companies some flexibility in terms of how to calculate taxable income in a given year. As a result, firms may not need to pay corporate income taxes (or only a little) for years after a mine begins production. To complicate matters, mining companies often operate in multiple jurisdictions: a firm may have a mine in Nunavut, another in Quebec, and headquarters in Toronto. Canada's tax laws establish how firms allocate their taxable income, which impacts how much they actually need to pay to the GN. As a firm's main goal is to generate profits, it will actively look for ways to reduce the amount of taxes it pays generally, across all jurisdictions. In short, even though a firm may generate significant revenues from its mine in Nunavut, it is not yet clear how this will translate to CIT revenues for the GN.

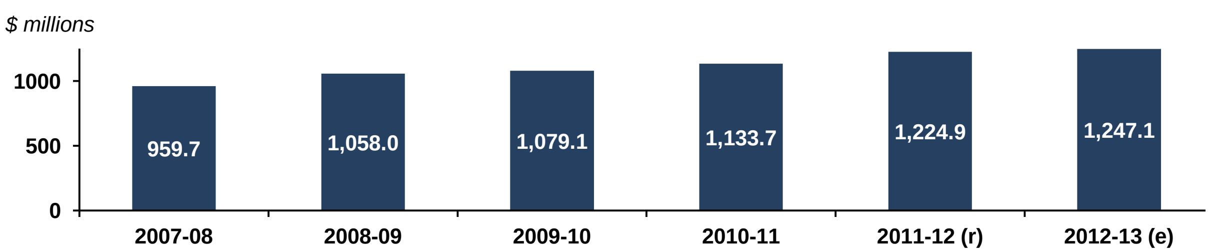
Expenditures

The GN has planned departmental expenditures of $1,341.6 million in 2012-13, which is $113.1 million lower than we projected to spend in the revised 2011-12 estimates. This includes $1,247.1 million for programs and services (operations and maintenance) and $94.5 million for capital. As noted above, it does not include spending made under third-party agreements or for non-appropriated expenses such as amortization.

Operations and Maintenance (O&M) Expenditures

The GN plans to appropriate $1,247.1 million for departmental O&M spending in 2012-13, $22 million (1.8%) more than we expect to have spent in 2011-12. This is a notably smaller increase than the 8% jump between 2010-11 actual spending and the revised 2011-12 estimates. Taking the two years together, O&M spending increased between 2010-11 and 2012-13 at an average of 4.9%, which is consistent with the longer term trend of about 5.4% average annual growth since 2007-08 (Figure 1-6). Put simply, relatively low O&M spending growth in 2012-13 may balance out the high O&M spending growth in 2011-12.

Figure 1-6: Historic O&M spending



As with other Canadian governments, the GN's Department of Health and Social Services (HSS) requires the most funding. In fact, the GN has planned for HSS to spend $316.7 million in 2012-13, 25% of the GN's entire O&M budget. The Department of Education, for which we have set aside $232.9 million in 2012-13, is the GN's second largest department in terms of spending. Community and Government Services and the Nunavut Housing Corporation are also relatively large, with planned expenditures of $188.1 million and $157.4 million respectively. Collectively, the remaining GN departments spend $352 million.

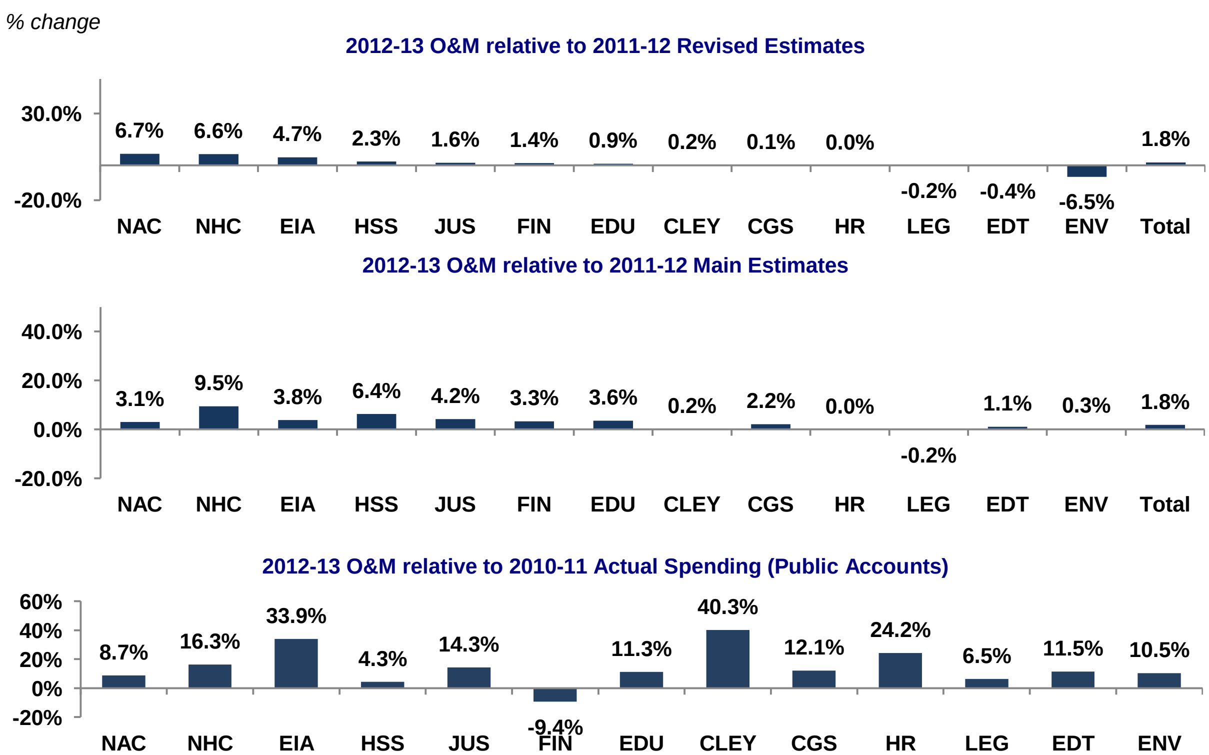
Supplementary Appropriations (O&M)

The Legislative Assembly approves Main Estimates each year, providing departments with the authority they need to spend taxpayers' money. If departments need to adjust their spending throughout the year the Legislative Assembly provides the authority to do so through Supplementary Appropriations.

At the time of writing, the Legislative Assembly had approved two O&M Supplementary Appropriation Acts in 2011-12, providing an additional $30.5 million in spending authority over the 2011-12 approved Main Estimates. Examples of the adjustments include an additional $7.3 million to help departments cover the impact of the Qulliq Energy Corporation's (QEC) 18.88% rate increase, effective April 1, 2011. The Department of Education received $5.7 million to fund a wage increase as a result of the new four-year collective agreement with Nunavut teachers, and HSS received $12.2 million to address anticipated cost pressures. These appropriations are fairly typical of the requests received throughout a regular fiscal year.

Overall, departments face similar O&M spending levels in 2012-13 as they received in 2011-12. All departments except the Department of Finance will receive more funding in 2012-13 than they actually spent in 2010-11 (Figure 1-7). Finance's 2010-11 spending included a $13 million payment to QEC to compensate the corporation for a one-year deferral in the implementation of the approved rate increases which took effect April 2011.

Figure 1-7: Changes in O&M Expenditures



Note: 2011-12 Revised Estimates only consider O&M Supplementary Appropriations 1 & 2.

Figure 1-8: Overview of GN Expenditures (Main Estimates basis)

$ thousands	Main Estimates 2012-2013	Revised Estimates[1] 2011-2012	Main Estimates 2011-2012	Actual 2010-2011
O&M Expenditures				
Office of the Legislative Assembly	16,898	16,935	16,935	15,873
Executive and Intergovernmental Affairs	20,785	19,843	20,020	15,520
Finance	63,200	62,354	61,177	69,737
Human Resources	24,120	24,120	24,120	19,414
Justice	92,085	90,676	88,387	80,576
Culture, Language, Elders and Youth	27,942	27,892	27,892	19,922
Education	232,895	230,711	224,765	209,298
Health and Social Services	316,677	309,690	297,758	303,504
Environment	22,353	23,908	22,278	20,237
Community and Government Services	188,127	187,953	184,098	167,871
Economic Development and Transportation	58,998	59,211	58,355	52,903
Nunavut Housing Corporation	157,382	147,576	143,759	135,267
Nunavut Arctic College	25,614	24,003	24,853	23,556
Total O&M Expenditures	**1,247,076**	**1,224,872**	**1,194,397**	**1,133,678**
Capital Expenditures				
Office of the Legislative Assembly	875	2,675	992	879
Executive and Intergovernmental Affairs	0	0	0	0
Finance	100	2,701	100	4,419
Human Resources	0	0	0	0
Justice	900	14,578	3,450	16,804
Culture, Language, Elders and Youth	60	898	7,060	3,687
Education	17,810	14,063	10,152	21,615
Health and Social Services	10,536	38,333	34,861	2,492
Environment	3,044	5,156	4,020	1,330
Community and Government Services	30,770	84,527	34,022	39,129
Economic Development and Transportation	14,400	19,006	3,925	7,953
Nunavut Housing Corporation	16,004	47,894	23,894	83,369
Nunavut Arctic College	0	0	0	0
Total Capital Expenditures	**94,499**	**229,831**	**122,476**	**181,677**
Total Expenditures				
Office of the Legislative Assembly	17,773	19,610	17,927	16,752
Executive and Intergovernmental Affairs	20,785	19,843	20,020	15,520
Finance	63,300	65,055	61,277	74,156
Human Resources	24,120	24,120	24,120	19,414
Justice	92,985	105,254	91,837	97,380
Culture, Language, Elders and Youth	28,002	28,790	34,952	23,609
Education	250,705	244,774	234,917	230,913
Health and Social Services	327,213	348,023	332,619	305,996
Environment	25,397	29,064	26,298	21,567
Community and Government Services	218,897	272,480	218,120	207,000
Economic Development and Transportation	73,398	78,217	62,280	60,856
Nunavut Housing Corporation	173,386	195,470	167,653	218,636
Nunavut Arctic College	25,614	24,003	24,853	23,556
Total Expenditures	**1,341,575**	**1,454,703**	**1,316,873**	**1,315,355**

1. At the time of writing, 2011-12 Revised Estimates reflect Supplementary Appropriations 1&2. We expect there will be an additional O&M Supplementary Appropriation for 2011-12.

Capital Expenditures

The GN has appropriated $94.5 million for new capital spending in 2012-13. Of this, CGS will receive $30.8 million, Education will receive $17.8 million, and the NHC will receive $16 million. The Departments of EDT and HSS will also receive significant amounts. Other departments will receive little capital funding, or none at all (Figure 1-8).

Capital carryovers *represent funds the GN approved in a fiscal year but did not spend in that year. This can occur when a project is delayed: the GN has authorized the spending but the project still needs to be finished. To ensure that payments are recorded in the same year that the work is completed (a fundamental accounting principle), the GN "moves" the money forward.*

Overall, the GN is devoting a significantly lower amount to capital than the $229.8 million that departments received in 2011-12. Of this amount, the GN provided $107 million of additional spending authority through supplementary capital appropriations during the 2011-12 fiscal year. In fact, most ($75.2 million) of the amount approved through 2011-12 supplementary appropriations represent "carryovers" from capital funding appropriated in 2010-11 or prior years. Before these supplementary appropriations and carryovers, the GN had appropriated $122.5 million through the 2011-12 Capital Estimates, which is more comparable with the $94.5 million appropriated for 2012-13.

The GN anticipates that it will carry forward $46 million from 2011-12 to 2012-13 through supplementary capital carryover appropriations. Carryovers represent capital funding the GN has previously approved but not yet spent. Added to the $94.5 million in newly-approved capital funding, the GN expects to authorize capital spending of about $140 million in 2012-13. Based on our experiences to date, it is likely that the GN will not spend all of this funding in 2012-13, and will need to carry forward some of it to 2013-14.

Capital carryovers are not uncommon within the GN for various reasons. For example, most construction materials must be transported by boat. As Nunavut's shipping season is relatively short, if materials miss a shipment or the ship is late projects can easily be delayed by weeks or months. If a shipment misses the last boat of the year (often leaving in September) projects may need to wait almost a full year before the materials can arrive the following season (often July in many communities). Capital carryovers can significantly impact GN spending figures in a given year—particularly when comparing estimated spending and actual spending—which in turn impact surplus or deficit forecasts. Accordingly, the GN presents its surplus/deficit estimates in ways that both include and exclude the impact of capital carryovers.

Territorial Debt and Borrowing Limit

As indicated in the notes of the 2010-11 Public Accounts, the GN had borrowed $105.2 million at March 31, 2011. This is $9 million higher than 2009-10, but is comparable to recent years. The GN reports borrowing as a whole, which means it includes the debts of its consolidated entities such as the QEC and the NHC.

Figure 1-9: Debt Cap Obligations	
$ thousands	
At March 31, 2011	
QEC Long Term Debt	73,500
NHC Long Term Debt	17,436
GN Mortgages Payable	3,894
QEC Bank Overdraft	24,000
NDC Subsidiary Credit Facilities	700
	119,530

Under the *Nunavut Act* the Government of Canada has capped GN borrowing at $200 million since 1999. The GN has taken a prudent approach to considering what types of borrowing to count against this limit. For example, the Public Accounts records actual debt the QEC, NHC and the Nunavut Development Corporation (NDC) have accessed. However, the GN guarantees higher levels of debt for these entities, and considers the full amount it guarantees under the borrowing limit. On this basis, the full obligations under our debt cap amounted to $119.5 million at March 31, 2011 (Figure 1-9). In November 2011, the GN agreed to increase the guarantee for QEC borrowing by $20 million, to $93.5 million, raising total borrowing under the debt limit to about $140 million at December 31, 2011.

Raising the Borrowing Limit

When used properly, debt helps governments spread the financial impacts of their decisions over time, which can allow for better planning and the potential for more efficient spending. However, debt can be dangerous if mishandled. A higher debt means a government must direct more public revenues to cover interest and other debt servicing costs, which in turn limits its ability to address other spending priorities. Taking on debt also increases a government's exposure to interest rate risk: debt that may seem quite affordable can become difficult to manage if interest rates rise significantly or unexpectedly.

With these benefits and risks in mind, the GN has asked the federal government to raise our debt limit. A higher limit would enable the GN to borrow funds to invest in key capital projects that are important for Nunavut's long-term economic growth. However, this would also increase the GN's borrowing costs—the amount of money the GN would need to pay to lenders to service the higher debt—which eat into other spending areas. We expect discussions with the federal government will wrap up in the coming months.

Fiscal Forecast

Revenue Outlook

The GN will continue to rely on the federal government for most of its revenue in the coming years. While federal transfers have provided the GN with fiscal stability and flexibility, our continued dependence on federal funding means that the GN's financial future is ultimately bound to decisions made in Ottawa. This understanding is particularly relevant as the GN and federal government begin to discuss the renewal of the major federal transfers, which are set to expire in 2014.

The GN expects its overall revenues to grow in line with the major federal transfers. When preparing its forecasts, the GN assumes its fiscal arrangements with the federal government will remain materially unchanged. This assumption is reasonable for the short-term, but may not be accurate for years beyond 2014.

Figure 1-10: Revenue Forecast

$ millions	Revised Estimates 2011-12	Main Estimates 2012-2013	Forecast 2013-2014	Forecast 2014-2015
Territorial Formula Financing	1,175.3	1,273.5	1,353.3	1,414.5
Other	75.5	82.6	81.0	71.2
Total Federal Transfers	**1,250.8**	**1,356.1**	**1,434.3**	**1,485.7**
Own-Source Revenues	**115.8**	**120.2**	**125.9**	**125.9**
Total Revenues	**1,366.6**	**1,476.3**	**1,560.2**	**1,611.6**

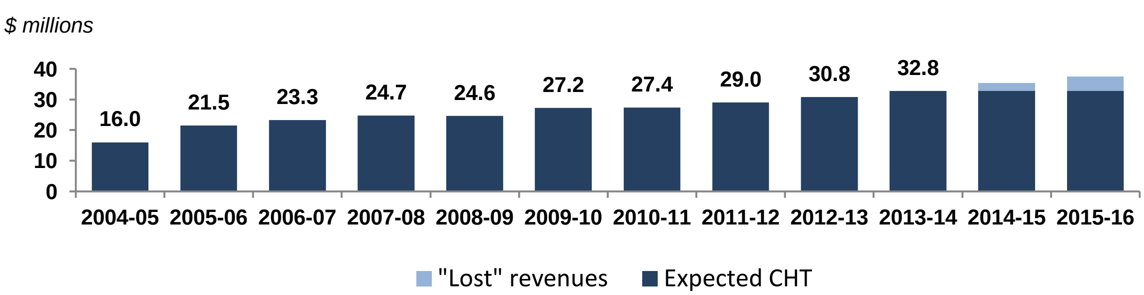
1. Does not include third-party revenues. Includes estimates of revolving funds (~18.5 million) in own-source.

Renewal of Federal Transfers

In December 2011 federal Minister of Finance Jim Flaherty provided a few insights into how the Government of Canada planned to deal with some of the major renewal issues. The key announcement was that the Government of Canada planned to change the way it calculates CHT payments. He confirmed that the national envelope—which determines how much money is divided among all Canadian jurisdictions—would continue to grow at 6% until 2016-17. He also said this rate was unsustainable, and announced that the envelope will grow in line with the economy—measured by nominal GDP—starting in 2017-18 (at a minimum of 3%). As economic growth will be notably lower than 6%, overall CHT payments will start to slow that year, which means less money for provinces and territories over time. As the CHT makes up only 2% of the GN's overall revenues the impact will not be as significant for us as it will be for some jurisdictions. This proposed change is particularly important for the provinces, which rely significantly more on the CHT.

Minister Flaherty also confirmed that starting in 2014-15 the federal government will allocate the CHT on an equal-per-capita basis, instead of using the existing formula. This change was initially legislated in 2007. It will negatively impact jurisdictions with small populations, including Nunavut. Minister Flaherty committed that no jurisdiction will see its CHT decrease, which means the GN's CHT grant is likely to stall at its 2013-14 level (~$32.8 million) before starting to rise again. Although funding will not go down, internal forecasts suggest the GN will "miss out" on about $2.6 million in 2014-15 and $4.8 million in 2015-16 due to the proposed change (Figure 1-11). The cumulative impact of not receiving these payments will add up substantially over time.

Figure 1-11: CHT likely to "stall" at ~$32.8 million until 2016-17 due to proposed changes



So far, early discussions with our federal, provincial and territorial counterparts regarding the renewal of the TFF have been collegial, and the GN looks forward to engaging with them further as we move towards the next understanding of what it means to be part of the Canadian federation. While we anticipate discussions to be generally productive, the Government of Canada has its own fiscal goals and constraints in mind.

This is why renewal discussions need to focus not just on a dollar figure, but also on understanding how to achieve what the TFF is intended to accomplish: providing the GN with enough funding to deliver the same type, scope and quality of public services that Nunavummiut deserve, at tax rates comparable to those facing other Canadians. As there is already a well-developed approach to defining and calculating comparable tax rates, we should now focus on understanding the other side of the equation—how to consider and define what it means to deliver public services in Nunavut that are comparable to those that other Canadians expect from their own provincial and territorial governments.

For this reason, and in keeping with the GN's emphasis on self-reliance, it is important that the GN does what it can to reduce fiscal dependence on the federal government. For the GN to become more fiscally self-reliant, it must expand its tax receipts and other own-source revenues. A tax system should be competitive to encourage economic growth. It should also be efficient, distorting market incentives as little as possible, and equitable, so that the taxpayers share the tax burden in a way that is not unjust to certain groups. With these principles in mind, the best way for the GN to increase its fiscal self-sufficiency is to help Nunavut's private-sector economy grow and diversify, rather than resorting to high tax rates or taxing specific sectors. As the private sector grows, personal and corporate income tax, payroll tax and property tax will likely have the most potential as significant own-source revenue streams, even without any rise in tax rates.

Expenditure Outlook

The GN expects expenditures to rise steadily over the medium term. Like many Canadian governments, the GN faces significant cost pressures. There are two keys issues that exacerbate Nunavut's expenditure needs.

First, the GN faces significantly higher costs than other provinces and territories. Some reasons are obvious, such as our vast geography, far-flung communities, tiny population, and harsh environment. Other reasons are less recognized but no less valid. For example, our small population means we lack the economies of scale and scope that other governments take for granted, and relatively low education, training and competition in the territory diminishes productivity. These more intangible factors drive costs higher.

Second, Nunavut is not working from the same starting position as other Canadian governments, particularly with respect to infrastructure. Infrastructure enables and facilitates private-sector growth and public-sector service delivery. Sufficient, modern, and well-maintained infrastructure can lower costs, increase output, and—for many types of public infrastructure—can increase quality of life (through ensuring clean water, safe homes, etc.). Infrastructure includes both traditional infrastructure (such as buildings and treatment plants) as well as modern infrastructure (such as reliable high-speed communications).

Meeting Nunavut's critical infrastructure deficit will cost several billion dollars. For these and other objective (though hard to quantify) reasons, the GN has significantly higher spending needs than our provincial—and even territorial—counterparts.

Despite this, total spending is set to decrease over the next few years based on the GN's current funding allocation (Figure 1-12). In large part, this reflects the GN's attempt at transitioning to a three-year expenditure forecast. Although we recognize the importance of budgeting over the medium term and are moving in this direction, many spending managers in have a difficult time forecasting beyond the next fiscal year, and so often understate out-year estimates. We are working to improve these estimates over time.

The decline in total expenditures also results from a drop in approved capital projects between 2012-13 and 2013-14, and from limiting O&M spending over the next two years to current levels. However, as current allocation does not capture future need, this will be quite difficult to accomplish in practice. The GN will continue to face large spending pressures, particularly for new capital projects across the territory. Although the GN has not yet allocated funds to these future (and currently unknown) capital projects, there is still an acute and obvious need to continue to invest in Nunavut's infrastructure.

Figure 1-12: Expenditure Forecast (Main Estimates basis)

$ millions	Revised Estimates 2011-12	Main Estimates 2012-13	Forecast 2013-14	Forecast 2014-15
Operational Expenditures	1,224.9	1,247.1	1,255.2	1,253.9
Capital Expenditures	229.8	94.5	97.5	74.7
Total Expenditures[1]	**1,454.7**	**1,341.6**	**1,352.7**	**1,328.6**

1. Does not include money set aside for contingencies or supplementary requirements.

Risks to the Fiscal Outlook

The primary risk to the GN's long-term fiscal health is tied to the TFF and the transfer renewal process, which could result in a decline (or, more likely, slower growth) in GN revenues. Although the Government of Canada is facing fiscal challenges of its own, Minister Flaherty has committed that the federal government would not reduce transfers to other levels of government. Minister Flaherty has also stated that the federal government does not plan to change the basic structure of the TFF upon its renewal. These statements are good signs for continued stable growth, but they are far from being "guarantees" regarding future TFF funding levels (nor do they preclude actually increasing the TFF to better reflect the GN's actual spending needs).

Short-term risks include the potential need for the GN to cover costs associated with extraordinary or unforeseen events, such as a failure of essential municipal infrastructure or environmental liabilities, such as an oil leak. To prepare for such events, the GN has prudently set aside $25 million in 2012-13 and $30 million in 2013-14 and future years.

Fiscal Management

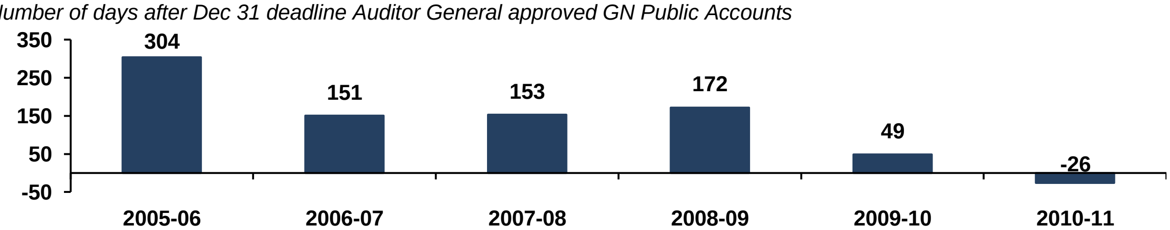
The GN is committed to achieving and following the highest standards of fiscal management expected of a Canadian government. As a young organization, we are working hard to develop and implement the knowledge, processes and internal infrastructure needed to catch up to our provincial and territorial peers in terms of fiscal planning, control and reporting. The GN has taken important steps in recent years, particularly with the support and assistance of Finance Canada and other federal departments and organizations.

For example, Section 44 of the *Nunavut Act* requires the GN to table its financial statements in the Legislative Assembly by December 31 each year. In an unqualified opinion dated December 5, 2011, the Auditor General of Canada formally reported the GN's 2010-11 consolidated financial statements published in the Public Accounts. The Commissioner of Nunavut accepted these statements on behalf of the Legislative Assembly prior to the statutory deadline.

This was the first time that the GN has complied with this particular reporting requirement. Although this may not seem especially noteworthy (other Canadian governments do it all the time) it reflects an important evolution within the GN. With internal hard work, targeted financial support from the federal government, and practical recommendations and support from the Office of the Auditor General, the GN has improved our financial reporting systems and controls, increased our collective understanding of public sector financial reporting, and demonstrated our ability and willingness to meet the standards expected of us. The results are evident. Between 2008-09 and 2010-11, we sped up our reporting process—measured by the number of days it took for the Auditor General to sign-off on the Public Accounts—by more than six months. We finalized our financial statements almost 11 months faster for the 2010-11 year than we did for fiscal year 2005-06 (Figure 1-13).

Figure 1-13: GN finalized its 2010-12 Public Accounts before the deadline for the first time

Number of days after Dec 31 deadline Auditor General approved GN Public Accounts



Fiscal Management Principles

As part of the GN's goal to meet the high fiscal management standards other Canadian jurisdictions have set, Cabinet recently directed GN Finance to develop principles for long-term planning and budgeting to restore and maintain the GN's fiscal resources.

We are in the early stages of determining what such a fiscal management strategy might look like, but expect it could include principles relating to debt management, balancing budgets, dealing with surpluses, and forecasting revenues/spending. We will also need to identify, track and publish specific financial indicators that will present a fuller picture of the GN's financial condition, such as net debt.

Fiscal transparency is one principle we plan to include in this strategy, and is an area in which the GN can improve. It is important for Canadian governments to be transparent about their spending decisions and about how they use and control public money and other public assets. Part of this means providing Nunavummiut and other stakeholders with the information they need to understand the GN's fiscal decisions, as well as its financial condition and performance. The information needs to be presented in ways that are accessible and appropriate for a range of audiences, from accountants to lay-people.

Publishing financial statements and other fiscal/financial reports on a timely basis is a good step forward. Future steps will include working to ensure that other documents—including this Fiscal Outlook—are easily comparable to the Public Accounts. This may take some time to achieve fully, as it will require modifying internal processes in terms of what information we track and forecast and developing new products, which requires resources (mostly time and people) that are in short supply. However, we are committed to moving steadily in this direction.

2 Economic Outlook

Highlights

- **Economy**. The Conference Board of Canada estimates Nunavut's real gross domestic product (GDP) was **$1,269 million in 2011**, up 6.8% from $1,188 million in 2010. This is strong growth, but is significantly less than what the CBoC had predicted last August.
- **Jobs**. The CBoC estimates employment in Nunavut reached **11,800 in 2011**, from 11,700 the previous year. Looking forward, the CBoC optimistically projects strong growth related to mining and construction.
- **Unemployment rate.** Nunavut's unemployment rate rose to 16.3% in 2011, from 15% in 2010 as about 400 people joined (or returned to) the wage economy.
- **Looking forward.** The global economy is highly unsettled, due in large part to concerns about the debt crisis in Europe. Like 2011, 2012 may be a bumpy ride.

Nunavut and Global Economic Developments

A bumpy ride

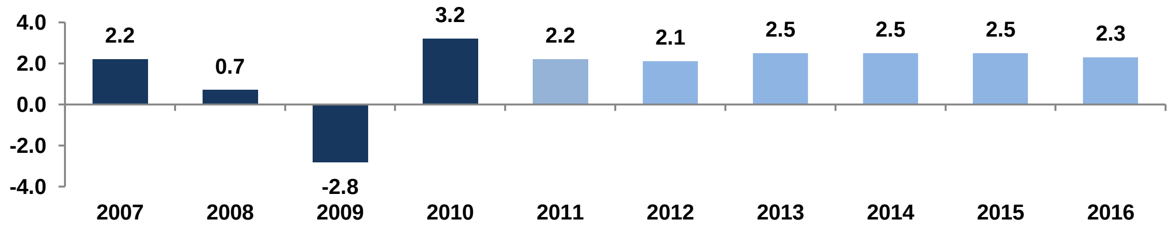
In January 2012, many of the world's leaders—representing industry, governments, academia and other areas of society—met in Davos, Switzerland, to participate in the World Economic Forum. They discussed a range of issues, from food security to how the internet shapes global growth. Whatever the topic, a common theme emerged: the global economy has had more downs than ups in recent years, and the bumpy ride is not yet over.

Canada's economy has recovered from the downturn triggered by the 2008 financial crisis, though tentatively. At first, Canada's economy fared moderately well, emerging from its brief put painful recession in mid-2009 and growing at a reasonable 3.2% in 2010. Government stimulus measures peaked and consumers played "catch up" with the purchases they had held back from making the year before.

Unfortunately, the momentum in 2010 was not enough to keep Canada's economy growing at that pace on its own. Governments withdrew their stimulus spending and shaky global events reminded businesses and consumers that the world economy remained fragile. Canada's growth slowed in 2011 to about 2.2%. Without any particularly good news on the horizon, many expect that 2012 will be similar. According to Finance Canada's September 2011 survey of private sector forecasters, Canada's economy will grow at about 2.1% in 2012, though there is some hope that growth will increase slightly in 2013 and beyond (Figure 2-1). The Bank of Canada projects a similar story in its January 2012 Monetary Policy Report, though with slightly different figures (2.4% in 2011, 2.0% in 2012, and 2.8% in 2013).

Figure 2-1: Historic and Forecast Real GDP Growth, Annual, Canada

% change year-over-year



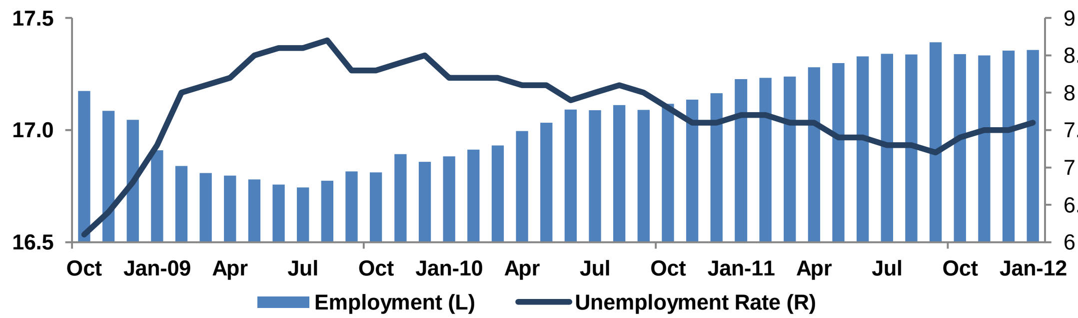
Source: Statistics Canada, 2007-10; Finance Canada (average of September 2011 private-sector predictions), 2011-16;

Recent data releases have not done much to brighten views. Statistics Canada data from January 2012 show that Canada's economy stalled completely in October 2011 and likely contracted slightly in November. This may mean annual growth in 2011 is even lower than the private sector projected in September.

Employment data has also disappointed. National employment rebounded noticeably in 2010, and by January 2011 Canada's economy had fully regained the jobs it had lost since its pre-recession employment peak in October 2008. Although 2011 started out well, adding 160,000 new jobs across the country before September, the last few months of the year were not as rosy. Canada actually lost 50,000 jobs in October, though there have been some small gains since. As of the Statistics Canada's February 2012 Labour Force Survey, there were about 130,000 new jobs in Canada in January relative to the year before. However, as more people look for jobs but cannot find them, Canada's unemployment rate has edged up, reaching 7.6% in January, the highest it's been since April 2011 (Figure 2-2).

Figure 2-2: Employment and Unemployment, Canada

Millions of jobs; percent



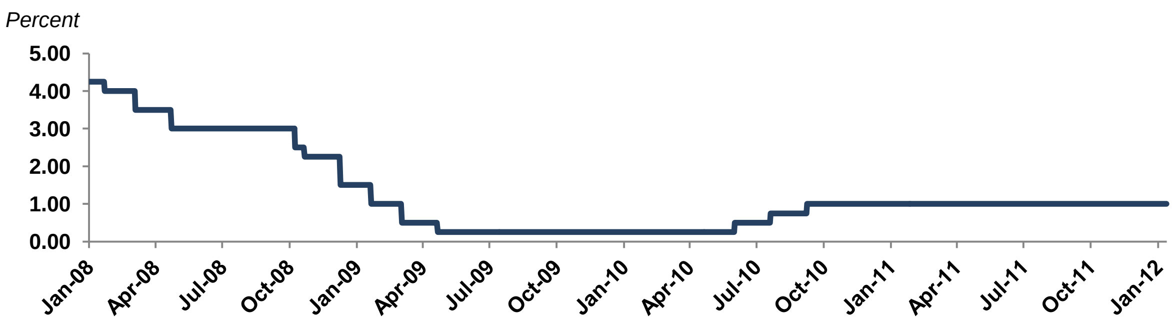
Source: Statistics Canada (Labour Force Survey)

International events over the past few months have contributed to Canada's hesitation. The Bank of Canada's opinions of the global economy have deteriorated since October, particularly as Europe's sovereign debt crisis has intensified and continues to create uncertainty across financial markets. What started out as an overspending issue among some European countries (notably Greece, but also Italy, Portugal, Spain, Ireland and others) has now spiraled into a European recession that is likely to be deeper and longer than many initially expected. The debt crisis has also called into question the fundamental structure and success of the European Union. Although European authorities are trying to implement sufficient measures to contain the crisis, many are skeptical that politicians will be able to make the difficult choices required of them. Just like the 2008 financial crisis spilled over from the US housing market to impact the world, this financial crisis could very well spill over Europe's own boundaries.

Elsewhere in the world, Chinese growth is slowing from what has been a tremendous rate over the past few years, which could negatively impact global commodity prices. Fortunately, it is not all bad news. The US, which is important for Canada's economy, grew more quickly than expected in late 2011, though may slow to a more modest pace going forward.

Here at home, the Bank of Canada continues to play an important role through its accommodative monetary policy. After drastically reducing its target overnight rate to just 0.25% in April 2009 in an effort to spur spending during the recession, the Bank has since raised its rate to 1.0%. The Bank confirmed it would maintain this rate at its most recent release of January 2012, reflecting its cautious view of Canada's uncertain economic health.

Figure 2-3: Bank of Canada Target Rate



Source: Bank of Canada

Nunavut's links with the global economy

The unsettled global economic environment could impact Nunavut's economy in two ways.

The first link is fairly indirect, but with potentially long-term consequences. The GN is Nunavut's most important employer, builder, and consumer. It injects much-needed wealth into communities through wages, social assistance, construction projects and service contracts. GN spending relies on federal fiscal transfers, notably the Territorial Formula Financing (TFF) grant, which is set to expire in 2014. The Government of Canada's own fiscal situation—which ultimately depends on the strength of Canada's underlying economy—will certainly influence renewal discussions. Finally, Canada's economy is closely tied to those of our trading partners as well as the global financial markets.

While this may seem like a tenuous series of linkages, if the global economy unexpectedly stumbles enough to trigger another downturn in Canada, it is quite possible that Nunavut will face a tougher time renegotiating a TFF agreement in 2014 that allows for continued and growing GN investment in the territory.

The second link is more direct. Nunavut's mining sector offers the most potential for jobs and growth in the territory. However, the sector is closely tied to global commodity prices. When the economy is doing well mining firms can expect to get a high price for their resources, which encourages them to invest in new projects. When the global economy is slow, or when the outlook is poor, commodity prices tend to decline and investors shy away from risky projects like mining. Because the gold, iron and other resources in the ground are not going anywhere on their own, mining firms have an incentive to delay investments until they anticipate a more favourable climate. This means Nunavummiut will need to wait longer before these mining jobs come to the territory.

The key message: Nunavut is insulated from world economic events because of our strong fiscal reliance on the federal government, but we are not immune.

Nunavut's Economic Output

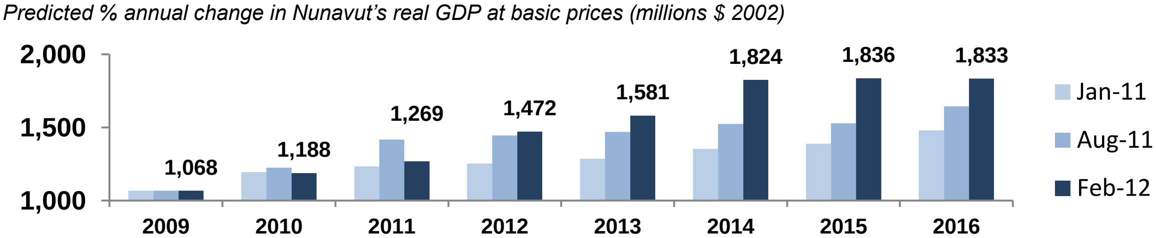
*The Conference Board of Canada releases a **Territorial Outlook** each summer and winter. At the time of writing, the CBoC had not yet published its Winter 2012 Outlook, though was in the process of revising its online data which the GN accesses through a subscription. We expect the CBoC will release their Winter Outlook in February 2012, and that it will explain the revisions to their August 2011 forecast figures.*

The CBoC estimates Nunavut's real GDP (measured in $2002) was $1,269 million in 2011, about $80 million, or 6.8%, higher than it was 2010.

This is solid growth, but reflects a substantial downward revision by the CBoC of its own August 2011 forecast, when it had predicted that the territory would expand by over $190 million, or more than 15%. This large revision highlights the uncertainty related to economic data and forecasting in Nunavut. We do not know the mechanics of the CBoC's model or reasons behind their revision. However, lack of data impedes all forms of analysis in the territory, and Nunavut's small size means that even slight modifications to assumptions (like whether a mine will start production in one year or the next) can result in large changes to forecast results. For these and other reasons, the CBoC regularly revises its estimates, both upwards and downwards (Figure 2-4).

Figure 2-4: Forecasts of real GDP evolve over time

Predicted % annual change in Nunavut's real GDP at basic prices (millions $ 2002)



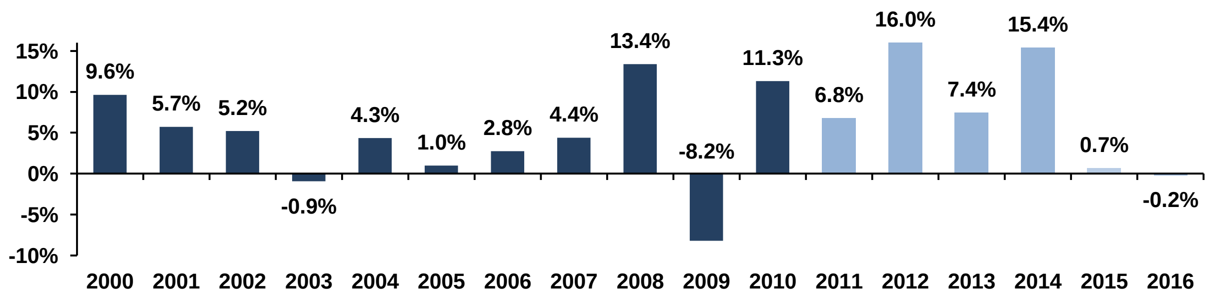
Source: CBoC Territorial Outlooks (Jan & Aug 2011) and database (Feb 2012)

Economic estimates for Nunavut (of GDP, employment, income, and other factors) will continually change until Statistics Canada confirms final figures, often a few years after the year in question has actually ended. Until then, estimates—including those by the CBoC—are simply projections, and should be understood as such.

Regardless of probable future revisions, 6.8% remains a high growth rate, particularly relative to other Canadian jurisdictions. Economic growth is good news, but Nunavut's small economy exaggerates year-over-year changes. For example, the CBoC's data indicate that real GDP grew over 13% in 2008, contracted by over 8% in 2009, and then had double digit growth in 2010. Looking ahead, the CBoC continues to project volatile growth, likely due to assumptions about future mining projects (Figure 2-5).

Figure 2-5: Annual growth is evident, but uneven

% annual change in Nunavut's real GDP at basic prices (millions $ 2002)

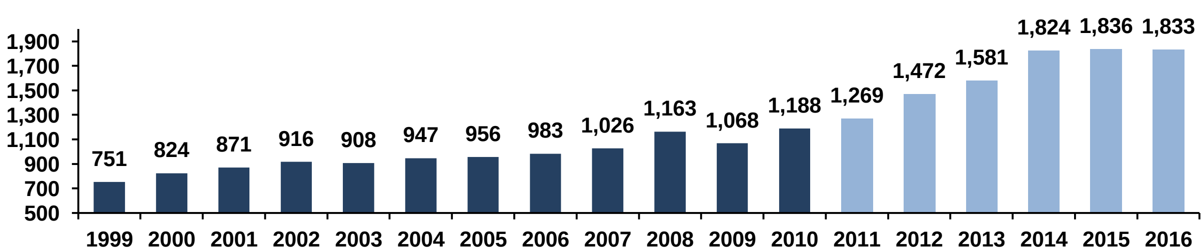


Source: CBoC Territorial Outlook Database (Feb 2012)

What matters most to Nunavummiut is that the economy grows over time, as this is a better reflection of increasing economic opportunity. Based on historic Statistics Canada data as well as CBoC projections, Nunavut's real GDP will have soon doubled in size, from about $750 million in 1999 to over $1.5 billion in 2013 (Figure 2-6).

Figure 2-6: Nunavut's real economy has expanded substantially since 1999

Nunavut's GDP at basic prices (millions $ 2002)

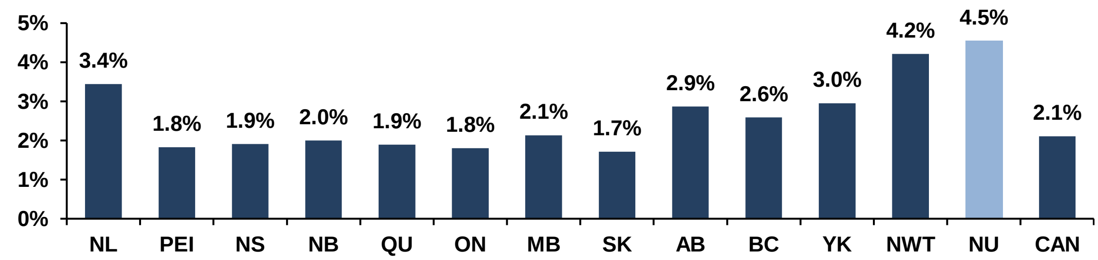


Source: CBoC Territorial Outlook Database (Feb 2012)

Statistics Canada data, which allow direct comparisons to other Canadian jurisdictions, show that Nunavut's real GDP expanded by about 4.5% each year between 1999 and 2010. This steady growth rate has outpaced those of all other Canadian jurisdictions over the same period (Figure 2-7). Based on the CBoC's forecasts, Nunavut's real economy will have grown by about 5.4% for each of the years between 1999 and 2016. Long-term growth will underpin job creation, individual wealth, and the GN's own ability to raise the own-source revenues used to deliver public programs and services.

Figure 2-7: Nunavut leads Canadian jurisdictions in historic average growth

Compound average growth rate of real GDP (1999-2010)



Source: Statistics Canada CANSIM Table 379-0025

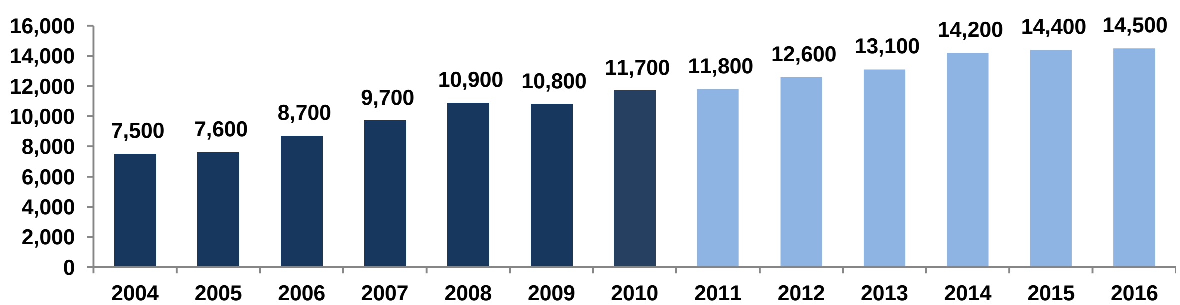
The mining sector was the largest contributor to growth in 2011, adding almost $40 million to territorial GDP (half the total increase). Growth in real estate, construction and transportation and warehousing contributed most of the balance. The CBoC projects that Public Administration's contribution to real GDP shrunk by about $4 million in 2011, though it is not clear why given GN spending that year was quite high.

Employment and Labour

Based on Statistics Canada's *Labour Force Survey*, the CBoC projects that about 11,800 individuals were employed in 2011, slightly more than the roughly 11,700 in 2010 (Figure 2-8). This particular survey does not reflect employment by non-residents, which is significant (particularly in industries such as mining and construction).

Figure 2-8: Historic and Forecast Approximate Employment

Number of individuals



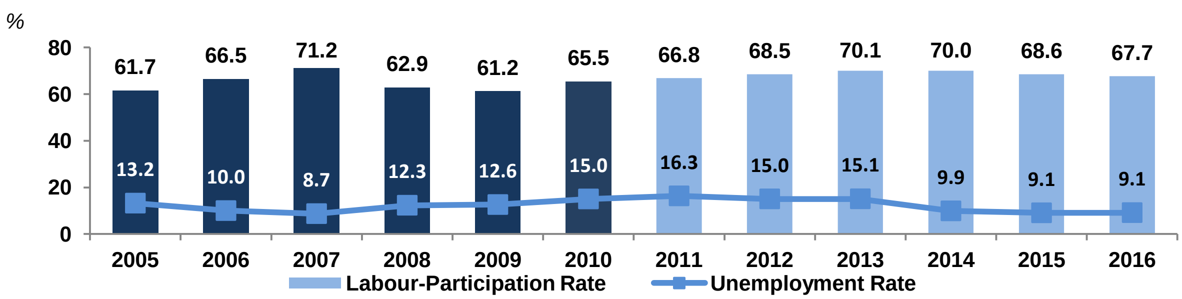
Source: CBoC Territorial Outlook database (based on Labour Force Survey data)(Feb 2012)

Looking ahead, the CBoC expects a substantial increase in employment for 2012, to almost 12,600 Nunavummiut. It is not immediately clear what is driving this increase, though the CBoC assumes mining will contribute almost 150 of the expected new jobs. The remaining new jobs are spread out among Nunavut's other sectors. This is a good sign; although mining is an important driver of growth and jobs in the territory, Nunavut's other sectors play expanding roles. Notably, the CBoC estimates that the number of jobs within public administration—the territory's largest employer—stalled (and may have even decreased slightly) last year, continuing the trend of slow employment growth in the sector. While governments will continue to be major employers in Nunavut, Nunavummiut will need to rely on the private sector to generate the majority of new jobs in the territory.

Unemployment and Labour Force Participation

Using data from Statistics Canada's *System of National Accounts*, the CBoC projects that Nunavut's unemployment rate rose to 16.3% in 2011, from 15% in 2010. This is due largely to an increase in Nunavut's participation rate, which reflects the share of Nunavut's working-age population (15+) who are either looking for a job or already have one. After reaching a low of 61.2% in 2009—at which point only three of five working-age Nunavummiut had a job or were looking for work—it has started to rise (Figure 2-9). The CBoC estimates another 400 people entered the labour force in 2011, though only 100 of them found a job.

Figure 2-9: Historic and Forecast Labour-Participation and Unemployment Rates



Source: CBoC Territorial Outlook database (participation rate based on Labour Force Survey; unemployment rate based on System of National Accounts)

There are many reasons why someone without a job might not look for employment. For example, they may be full-time students or elders who have retired from the workforce. There are also other less-constructive reasons. Perhaps an individual is too sick to work, or need to stay home to care for a sick or young family member, despite wanting a job. Others may simply be too discouraged to seek employment, so have given up trying.

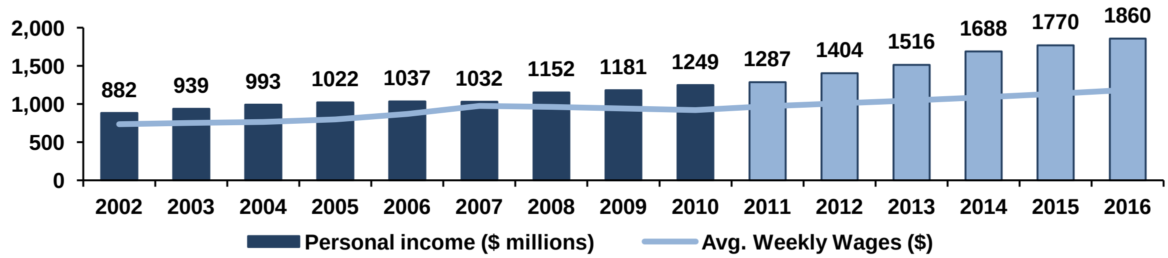
According to data from the Nunavut Bureau of Statistics and Statistics Canada, Nunavut's participation rate is regularly less than that of other Canadian jurisdictions, reflecting low participation by Inuit. By definition, participation rates measure involvement in the wage economy, and likely fail to capture participation in traditional activities such as hunting or crafts, despite the fact that these activities contribute to a healthy economy and, for Inuit especially, take the place of a wage-earning job. Nevertheless, there are likely deeper reasons behind the gap in participation rates between Inuit and non-Inuit. Increasing the involvement of Inuit in the wage economy remains key to Nunavut's economic development.

Looking forward, the CBoC is hopeful that the territory's participation rate will rise to 70% as more opportunities to work become available. Unfortunately, simply because people look for a job does not mean they will find one. Nuanvut's high unemployment rate—about more than double the national average—shows that many people in the labour force are actively looking for a job but cannot find one. There may simply be too few jobs in the economy, or perhaps individuals are not willing to move to the communities with employment opportunities. Often, there are many jobs available, but individuals do not have the skills needed to work in them. Still, the CBoC remains optimistic, projecting a drop in the unemployment rate to about 9%, comparable to 2007.

Economic growth has translated into steadily higher personal income, which has increased at about 4.1% each year for the past five years, which is more than inflation (Figure 2-10). Total personal income does not on its own determine wealth or standard of living. The high costs of northern living mean that Nunavummiut need relatively high income to meet basic needs, such as food and housing. Also, total personal income does not capture how the income is spread across the population.

Figure 2-10: Higher personal income and weekly wages

Total personal income ($ millions); average weekly wages ($)



Source: CBoC Territorial Outlook Database

Key Economic Sectors

There are two principal sources of economic growth in the territory: federal transfers and natural resource development. We discuss these impacts, as well as those of other key sectors, below.

Public Administration

Although economic growth is not the primary goal of most federal transfers, they have important impacts nonetheless. The reliable and steadily-growing federal transfers that flow into Nunavut provide the local economy with a base upon which to build. Federal transfers, which generally flow to Nunavummiut through the GN, provide a valuable source of funds that enter Nunavut's economy through wages, capital investment, government services, and local business contracts. As a result, government activity heavily influences economic growth, employment and investment in Nunavut.

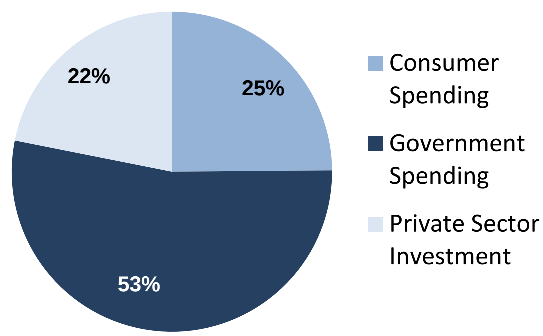
According to the CBoC, public administration—which includes municipal, territorial and federal government activities—contributed almost $280 million to real territorial GDP in 2011. The sector has actually contracted by over 4% since its contribution to real GDP peaked at almost $290 million in 2008.

Governments are also Nunavut's most important employer. The CBoC estimates the sector employed about 3,000 individuals and paid about $240 million in wages in 2010, roughly 25% of all wages paid in the territory that year. This level of government activity is significantly higher than in other jurisdictions.

The CBoC expects that governments, through their spending on goods, services and infrastructure, will contribute over $1.5 billion to Nunavut's economy in 2011, over half of all spending in the territory that year in terms of final domestic demand (Figure 2-11). Such a high contribution by governments impacts Nunavut's economy in many positive ways. Unfortunately, there are also negative aspects to high government involvement in the economy.

Figure 2-11: Contributions to Economy

% share of final domestic demand, 2011



Source: CBoC Territorial Outlook

Too high an involvement can stifle private sector growth, which is where Nunavut's true potential lies. Private sector growth is important because of its potential to generate new wealth in the territory, instead of simply shifting tax dollars from one person to another. If a government hires individuals who could have otherwise contributed to the private sector, or provides a good or service that the private sector could provide, it may "crowd out" valuable business opportunities. Of course, there are many essential activities in which governments do have a primary role, such as education and health care, which are important contributors to Nunavut's economy on their own, accounting for another $210 million of territorial GDP in 2011.

Mining and Petroleum

Natural resource development is the territory's other large driver of economic growth. The CBoC estimates that mining's contribution to GDP was $213 million in 2011, about $40 million or 23% higher than it was in 2010. This reflects the ramping up of Agnico-Eagle's Meadowbank gold mine as well as an increase in mining services across the territory.

Meadowbank began producing in 2010, driving territorial GDP higher by about $160 million. Economists often use GDP to tell a story of economic growth (specifically, the change in the total value of what an economy produces) but it tends not to mean much to most people. Nunavummiut, as other Canadians, care more about what economic growth means for jobs and communities.

The CBoC estimates that mining employed almost 500 Nunavummiut in 2011, and will pay out about $50 million in wages. This works out to roughly $100,000 per year for individuals working in the industry, more than similarly rough estimates for construction (about $90,000) and public administration (about $80,000). These calculations do not take into account a number of factors or data a full compensation analysis requires. However, they do serve as a very rough 'back-of-the-envelope' illustration of the potential that mining offers Nunavummiut. Individuals with the skills and abilities mining employers demand have substantial opportunity in the years ahead.

The recent surge in growth and jobs is attributable largely to Agnico-Eagle's Meadowbank gold mine, near Baker Lake, which started production in 2010. Nunavut has more projects waiting in the wings. According to the Department of Economic Development and Transportation, mining firms advanced several projects over the past year, including the Back River gold deposits owned by Sabina Gold and Silver Corp., the Hackett River silver-rich base metal deposit acquired by Xstrata Zinc Canada Ltd., the Meliadine gold deposit owned by Agnico-Eagle Mines, and the high-grade iron Mary River property owned by Baffinland/ArcelorMittal. A number of other projects—gold, diamonds, base metals, copper, gems—are in various stages of exploration.

There are risks inherent to being an economy that relies on mining. Mining is a highly capital-intensive industry, which means it relies on favourable credit and investment conditions. By its very nature, it is tied to global commodity prices, which are cyclical and potentially quite volatile. As noted above, the current global outlook in the short-term is highly uncertain. For these and other reasons, the timing of mine projects is far from certain, and projects can easily be delayed by a year or more. As an example, Newmont Mining Corp. recently announced that it is postponing development and surface exploration activities at its Doris North project in the Hope Bay region south of Cambridge Bay.

Despite these real risks, the long-term outlook for mining in Nunavut (and therefore Nunavut's private sector overall) is positive. In its August 2011 Territorial Outlook, the CBoC agreed, saying much about the driving role that mining will play in the territory (Figure 2-12). It will be interesting to see whether and how the CBoC's views will change in their next Outlook (expected February 2012) due to the events over the fall.

Figure 2-12: Mining in Nunavut, according to the CBoC

- "Ongoing mining developments and continued exploration of Nunavut's vast untapped natural resources will provide further impetus for growth."
- "Nunavut's largely untapped resources will result in another year of busy mineral exploration."
- "The territory's impressive mineral wealth continues to attract attention."
- "The wholesale and retail trade industries will benefit from increased mining activity and a burgeoning population of workers. In 2011, real demand for consumer goods is expected to grow 5.6%."
- "More mining output will require more warehousing and transportation services. Warehousing and transportation industries will grow by more than 45% over the next two years due to higher production at Meadowbank and the new development at Hope Bay."
- "The Mary River iron ore project has the potential to be one of the world's largest iron ore mines. It has been described as 'quite possibly the best undeveloped iron ore deposit in the world'."

Source: CBoC August 2011Territorial Outlook

Looking ahead, we expect mining—and in the very long-term, oil and gas—to attract billions of dollars in private investment, and provide well-paying jobs across communities to those with the skills employers need. Nunavut's petroleum industry has large proven and potential resources within the territory's borders. Still, the undeveloped state of the industry and the isolation of these resources make development economically unfeasible in current markets. It may take decades before the economic benefits of oil and gas development can be fully realized.

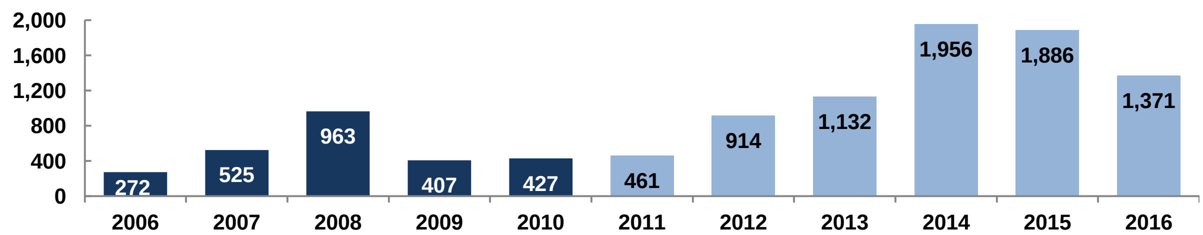
Construction

The CBoC estimates that construction contributed $191 million, or 15%, to territorial GDP in 2011. This is a $15 million increase from the previous year. While construction activity declined significantly in 2009, the sector's projected growth in 2011 and 2012 means its contribution to GDP could soon surpass peak 2008 levels.

These changes emphasize the somewhat volatile nature of the sector. Although construction is cyclical in many jurisdictions, following the broad ups and downs of the wider economy, Nunavut is small enough that a single large capital project can impact territorial data. For example, business investment in non-residential fixed capital began to rise steadily in 2006, likely reflecting early activities at the Meadowbank mine. As construction of the mine wound down in 2009, overall investment also fell (Figure 2-13).

The trough continued in 2010 and 2011, but the CBoC expects investment to increase substantially in 2012, and to jump again in 2014. Although these data reflect business investment in all areas of the economy, we expect these jumps to be due to CBoC assumptions about construction at mining projects.

Figure 2-13: Business Investment in Non-Residential Construction, Nunavut
$ millions



Source: CBoC Territorial Outlook database

According to the CBoC, Nunavut's construction sector employed about 730 people in 2011; over 6% of total territorial employment. This is consistent with the level of employment in the construction sector across Canada.

The *Construction Sector Council*, a national organization that studies the workforce needs of Canada's construction industry, forecasts the demand for construction jobs will increase steadily across the provinces and across trade occupations (carpenters, equipment operators, plumbers, etc.). Although they do not publish data for the territories, we expect that Nunavut will be no exception.

The high demand for construction workers presents challenges and opportunities for Nunavummiut. There is substantial opportunity for those who have adequate skills, or who are willing and able to acquire them. Not only could skilled workers find well-paying jobs within Nunavut, but they would also have substantial opportunities elsewhere in Canada. On the other hand, if there are too few skilled workers within Nunavut (which is currently the case), employers will have an increasingly difficult time attracting skilled workers from other provinces as demand in those provinces rises. This will mean local employers will be forced to increase wages even further to attract skilled workers from elsewhere.

Real Estate

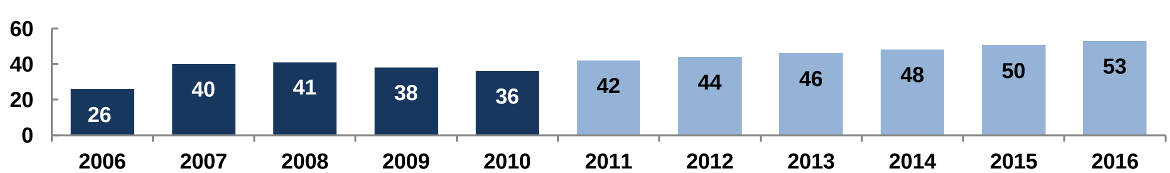
The CBoC reports that Nunavut's real estate industry, which is based on the development and leasing of commercial and residential properties, contributed $193 million, or 15%, of GDP in 2011. These figures include finance and insurance activities, which we expect are small relative to real estate. Contributing to this total are Nunavut's high rent prices and large and steady demand from the public sector, primarily the GN.

At the national level, Canada's real estate markets are on potentially shaky ground. Relatively cheap borrowing in recent years has made it easy for Canadians to borrow large amounts of money, which in turn makes it easier to pay more for housing and drive up house prices. In a recent report the International Monetary Fund warns that Canada's average home prices may be about 10% higher than they should be. To make things worse, the cheap borrowing has encouraged many Canadian families to take on more debt than they may be able to handle in a higher interest rate environment, leaving them vulnerable to either a rise in interest rates or a fall in house prices.

In Iqaluit, the strong demand for housing far outstrips its short supply, keeping home prices high, rental vacancies low, and the likelihood of widespread devaluation quite small. According to the Canada Mortgage and Housing Corporation's (CMHC) 2011 Northern Housing Report, the latest available, the average price of a single-detached home sold in 2010 was about $338,000, or roughly $213 per square foot. Condos, row houses or semi-detached sold for about $185 per square foot. For renting, the average two-bedroom unit rented at about $2,265 per month in 2010. This high rate reflects the high demand; for every 500 available units in Iqaluit in 2010, only two were available at any given time.

Figure 2-14: Business Investment in Residential Construction, Nunavut

$ millions



Source: CBoC Territorial Outlook database

Based on recent estimates, residential investment may have surpassed the 2008 peak in 2011. The CBoC expects investment in residential construction to rise steadily (Figure 2-14).

Tourism and Culture

With its unique culture and beautiful land and waters, Nunavut has much potential as a tourist destination, including for business travelers who add leisure days to their trips. However, the territory's private and public sectors will need to address a number of obstacles before it will be able to fully realize this potential for growth.

For example, many Canadians find it cheaper to fly abroad than it is to fly to Nunavut. The high costs of staying in Nunavut's hotels also turn many budget-minded travelers away. As another obstacle, Nunavut (particularly in the communities) lacks the amenities, activities and products that many travelers look for. Where they do exist, they are not always easy to find and it is not always clear to potential customers what to expect. Contributing to this lack of product there are few tourism professionals in Nunavut, limited training opportunities, and short tourist seasons.

These obstacles are manageable with private-sector entrepreneurship and some smart and targeted government support. The GN is developing a tourism strategy that will help create the conditions for growth. Ultimately, the GN can only do so much: it will be up to Nunavummiut to take advantage of the many opportunities that exist in the sector.

Tourism is closely connected with the arts and crafts industry, as they are both sectors where the value and potential lies within Nunavut's rich culture and identity. They also both represent opportunities for employment and income generation in Nunavut's smaller communities, outside the government hubs.

Fishing, Sealing and Harvesting

Fisheries are an important resource, and one with good growth potential. Nunavut's commercial fishery depends mainly on turbot, which had a landed value of $70 million in 2011. Shrimp (valued at $10 million) and Arctic char (with commercial sales of $1 million) are also important. Nunavut's fisheries sector continues to stake claims in Canada's commercial fishing industry by purchasing licenses and new vessels and by exploring Nunavut's waters. With support from the federal government, the GN recently purchased an advanced research vessel—the *Nuliajuk*—that will allow scientists to collect information on marine species, habitat, and populations within the Nunavut Settlement Area.

The sealing and harvesting sectors are important for Nunavut's communities, particularly as a source of nutritious food. The GN's Department of Environment estimates the food replacement value of seals to be over $5 million each year. To support harvesters, the GN purchases seal skins, tans them, and sells them back to Nunavummiut to be manufactured into arts, crafts and garments for domestic use and commercial sale. Long fur harvesting continues to be profitable, particularly as pelt prices are at record high levels for arctic fox, polar bear and wolf.

Harvesting caribou, seals and other animals is still mostly done as traditional subsistence hunting, meaning the meat is consumed within the hunter's family, shared among the community and only occasionally sold, either to other communities where the animal is scarce or, particularly in Iqaluit, through increasingly popular country food markets.