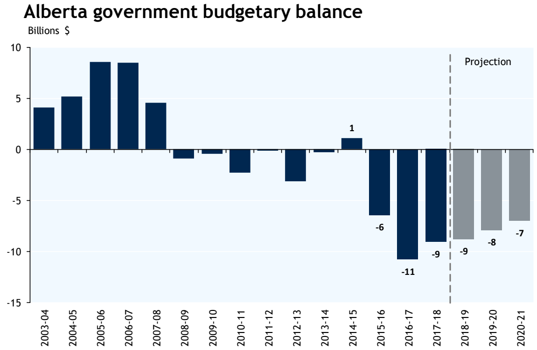
ALBERTA BUDGET 2018

March 23, 2018

Alberta government budgetary balance



Source: RBC Economics Research, Alberta Finance and Treasury Board

Table 1: Economic Assumptions					
Year-over-year % change	Forecast				
	2017	2018	2019	2020	2021
2018 Budget					
Real GDP growth	4.5	2.7	2.5	2.4	2.6
CPI	1.6	2.1	1.9	2.0	2.0
Nominal GDP growth	6.8	4.7	4.3	5.6	6.0
Unemployment Rate*	7.8	6.8	6.2	5.7	5.3
Employment growth	1.0	2.0	1.7	1.8	1.6
WTI ($/bbl)*	48	54	59	60	63
RBC Economics					
Real GDP growth	4.2	2.2	2.0		
CPI	1.5	1.8	1.8		
Nominal GDP growth	8.3	4.5	4.2		
Unemployment Rate*	7.8	6.9	6.5		
Employment growth	1.0	1.5	1.2		
WTI ($/bbl)*	51	54	56		

*Average level

Highlights

- Budget 2018 implied little change to the fiscal plan as outlined in Budget 2017 with the provincial deficit continuing to trend gradually lower through the four-year forecast period now ending in FY20/21.
- The government continues to indicate the elimination of the deficit by FY23/24 though frustratingly provides only a broad outline as to how such will be achieved.
- Revenues in FY17/18 came in stronger than expected in part due to greater resource revenues. The government used half of these savings to lower that year's fiscal deficit to $9.1B from the $10.5B projected a year ago using the other half to boost expenditures.
- The government is projecting the deficit dropping further in FY18/19 despite a falloff in resource revenues reflecting a widening gap between Western Canadian oil prices and global oil prices. The Alberta government opted to accelerate the scaling back on capital expenditure projects in FY18/19 thus providing an offset via lower expenditure growth.

Overview

Alberta's fiscal plan has changed very little relative to what was presented in Budget 2017 with limited new initiatives on either the tax or expenditure side being proposed. As a result, the government continues to forecast a gradual reduction in the deficit with its eventual elimination projected in FY23/24. However, it continues to be disappointing that this return to balance remains largely aspirational with the Alberta government only providing a very broad outline as to its fiscal strategy to achieve such.

The projected shrinking of the deficit through FY20/21 is helped by rising non-renewable resource revenue over the four-year forecast horizon from FY17/18 to FY20/21 though the growth rate has been halved relative to what was indicated in Budget 2017 (over the period FY16/17 to FY19/20). Generally the downward trend in the deficit is maintained by both higher non-resource revenue growth and a lower pace of expenditure increases. The higher revenue growth is in large part coming from stronger personal income tax revenue and a higher level of federal government transfers. On the expenditure side the main change resulted from a reduction in capital spending and attendant lowering in capital grants through the forecast period.

Budget 2018 does indicate smaller deficits in both the fiscal year just ending (FY17/18) and the upcoming fiscal year (FY18/19) relative to last year's budget dropping to $9.1B from $10.5B and to $8.8B from $9.7B, respectively. The improvement in FY17/18 resulted from revenues coming in $2.0B higher. This boost reflected both higher resource revenues

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($0.8B) along with a jump in investment income ($0.9B). The government did use half of these savings to boost expenditures by $1.0B in FY17/18. However, the government used the other half of the upward revenue surprise to lower the FY17/18 deficit along with the unused FY17/18 risk adjustment factor of $0.5B.

The challenge for the upcoming FY18/19 deficit are indications that non-renewable resource revenue, after a stronger-than expected increase in FY17/18, is poised to move lower in FY18/19. The shortfall was attributed to the widening spread between the world oil price (WTI) and the Western Canadian price (WCS) that resulted from constraints being encountered in both pipeline and rail capacity to move product to market. Revenue was still projected to increase by 2.1% in FY18/19 benefiting from continued solid nominal GDP growth in the province boosting revenues in areas such as personal income taxes. However this increase in overall revenues was down from the 5.8% increase projected a year ago. The offset was the Alberta government cutting expenditure growth in FY18/19 to only 0.5% from the 3.3% increase projected a year ago. A key contributor to the lowering in expenditure growth was the government decision to start scaling back its capital expenditure program more aggressively than indicated in Budget 2017. These savings helped the government to continue to show the deficit moving lower in FY18/19.

Budget Balance Profile

Budget 2018 reconfirmed the Alberta's government commitment to put the deficit on a downward trajectory. From the $10.8B recorded in FY16/17, the deficit dropped more than previously projected to $9.1B in FY17/18 benefitting from a solid jump in resource revenues of almost 50%. The pace of improvement is projected to slow in FY18/19 to $8.8B with the drop in the deficit being hampered by indications of some retracement in resource revenues from FY17/18's robust increase. Beyond FY18/19 the deficit continues to trend lower to $7.0B in FY20/21 with the government projecting strong revenue growth easily outpacing increases in expenditures. Budget 2018 did show a deficit profile out to FY23/24 that indicated a cessation of deficits with the balance showing a slight surplus of $0.7B.

Revenues

In Budget 2018 average annual revenue growth over the forecast period FY17/18 to FY20/21 has been raised to 6.3% from the 5.1% average increase projected last year over the forecast period FY16/17 to FY19/20. Increases in non-renewable resource revenue is a key contributor with growth averaging a strong 14.9% over the forecast. However, this increase is about half the 27.8% projected in Budget 2017. The downward revision in growth is in part due to indications of a widening gap in Alberta versus world oil prices that has resulted from Alberta producers having increased difficulty in the current environment to move product to market because of capacity constraints in both pipelines and rail transport. The Alberta government suggested that even this lower growth was contingent on increased pipeline capacity coming on stream by 2021 and thus the desire to see the contentious Kinder Morgan TransMountain Pipeline being competed on schedule.

The slowing in resource revenue growth is offset by the assumption of strong annual revenue growth outside of this component of 5.7% that compares to the 3.3% indicated a year ago. This in large part reflects average annual revenue growth from personal income taxes being doubled to 4.1% from the 1.7% projected a year ago. This in part can be explained by an upward revision to provincial GDP growth in 2017 and 2018 though it is not clear what maintains this higher growth in the out-years.

Expenditures

The downward trend in the Alberta government deficit over the medium term is also a reflection of average annual expenditure growth being reduced to 3.0% from the 4.4% projected in last year's budget. This slowing is achieved despite growth in operating expenses being held relatively steady at 3.0% compared to growth of 2.9% projected a year ago. This reflects the government's commitment to maintaining appropriate spending in key areas such as health and education. This includes providing incremental boosts to spending in a myriad of programs related to, for example, addiction and mental health, affordability of child day care and school meal programs.

The reduction in expenditure growth is largely achieved by the government more aggressively scaling back its capital expenditure program along with ongoing efforts to keep public sector compensation under tight control.

Net Debt

The persistence of deficits through the medium term contributes to Alberta's provincial net debt continuing to rise over this period from $20.3B in FY17/18 to $48.2B in FY201/21. As a share of GDP the ratio rises from 6.0% to 12.4% though even this terminal value represents a low ratio compared to most other Canadian provinces. This largely reflects the province being essentially debt free prior to the recent plunge in world oil prices and the attendant downturn in the Alberta economy in 2016.

Borrowing Requirement

The Alberta government expects its total financing requirements (i.e. for capital and fiscal plan purposes, and for provincial corporations, net of maturities) to decline from $17.3 billion in FY17/18 to $11.7 billion in FY18/19, and then rise slightly to $12.6 billion in FY19/20 and $12.2 billion in FY20/21. The government forecasts to issue long-term debt totaling $15.4 billion in FY18/19, $17.6 billion in FY19/20 and $17.5 billion in FY20/21.

Table 2: Alberta Fiscal Plan (billions of dollars)

	Forecast	Estimate		
	2017-18	2018-19	2019-20	2020-21
Non-Renewable Resource Revenue	4.5	3.8	4.2	5.0
Other Revenue	42.3	44.1	46.4	48.8
Total Revenue	**46.9**	**47.9**	**50.6**	**53.8**
Departmental and Other Expenses	54.6	54.3	55.4	56.9
Public Debt Charges	1.4	1.9	2.4	2.9
Total Expenses	**55.9**	**56.2**	**57.8**	**59.8**
Risk Adjustment		-0.5	-0.7	-1.0
Balance	**-9.1**	**-8.8**	**-7.9**	**-7.0**
Net Financial Assets	-20.3	-30.5	-39.8	-48.2
Total Borrowing Requirements	17.3	11.7	12.6	12.2

*based on government estimates

Source: Alberta Treasury Board and Finance