

Waiting and Hoping Alberta's 2017 Budget

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2017 Provincial Budget Post-Mortem

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Budgets Speak Volumes

- Don't tell me your values. Show me your budget and I will see what your values really are.

(Statement attributed to Joe Biden)

Hoping for a Return of Oil Prices



Governing is Tough

- Fine to blame former regimes for overspending and mismanagement of unprecedented oil and gas revenue.
- But what are you doing to deal with the fiscal threats facing the province?

Same Old Same Old

- This administration has the same vision of previous administrations: “Please god make there be another oil boom”.
- Government still talks in terms of cyclical factors – we have to spend big now to cushion economy before good times return.
- World has changed!

Cyclical vs. Structural

- Cyclical related to business cycle. Assumes economy and finances will return to more or less “normal” after a year or so.
- That has worked in the past which has benefited previous governments.
- Times have changed. Now dealing with structural or semi-permanent changes. The “new normal” may be worse than before. Resource revenue won’t return to previous levels.

Structural Factors

- Fracking in shale formations. In 2005-06 natural gas and by products over \$8 billion forecast for 2016-17 is \$219 million.
- Higher global oil supply at lower cost.
- Moving to a lower carbon world! Producers not in charge.
- Already used up PIT and corporate tax room.
- Growing debt to finance.

King Bitumen

By 2019-20 bitumen will account for 80% of non-renewable resource revenue.

	2017-18	2018-19	2019-20
Bitumen	\$2.5 billion	\$3.2 billion	\$5.3 billion
Other Res Rev	\$1.3 billion	\$1.0 billion	\$1.3 billion
Total NRRR	\$3.8 billion	\$4.2 billion	\$6.6 billion

Northern Boom Gone

- Boom town Fort McMurray shaped thinking of Alberta. But future not like the past.
- “Even with modest growth, non-conventional investment in 2020 is expected to be less than half of what it was in 2014. In part, this reflects the leveling off of capital spending already underway following the 2010-14 period, when spending more than tripled from 2009 levels.” Budget 2017 Economic Outlook

Bitumen Production

- There will not be enough pipeline capacity to accommodate oil sands production by early 2018 according to Budget 2017.
- Increased cost of rail will widen the L/H differential.
- Budget assumes Enbridge Line 3 in 2020 and KM Trans Mountain Expansion in 2021.
- How realistic are these timeframes?

High Sensitivities Increase Risk

1 % point increase in interest rates	-230 million
1\$ decrease in WTI	-310 million
\$1 increase in light/heavy differential	-285 million
1 cent increase in exchange rate	-215 million
10 cent reduction in natural gas	-25 million

Unstable Revenue Base

- Steadily declining revenue to GDP.
- Apart from pit and cit don't have dynamic revenue sources that grow with economy.
- Of \$44 billion revenue for 2017-18, 48% will come from taxes, 8% from resource revenue.
- 18% of Alberta's revenues will come from federal transfers or double the amount from resource revenue.

Revenue Expenditure Mismatch

- Two most dynamic revenue sources – personal and corporate taxes – don't cover health spending.

	2015-16	2016-17	2017-18
Personal and Corp Taxes	\$15.5 b	\$14.8 b	\$15.1 b
Health	\$20.0 b	\$20.7 b	\$21.4 b
Shortfall	-\$4.5 b	-\$5.9 b	-\$6.3 b

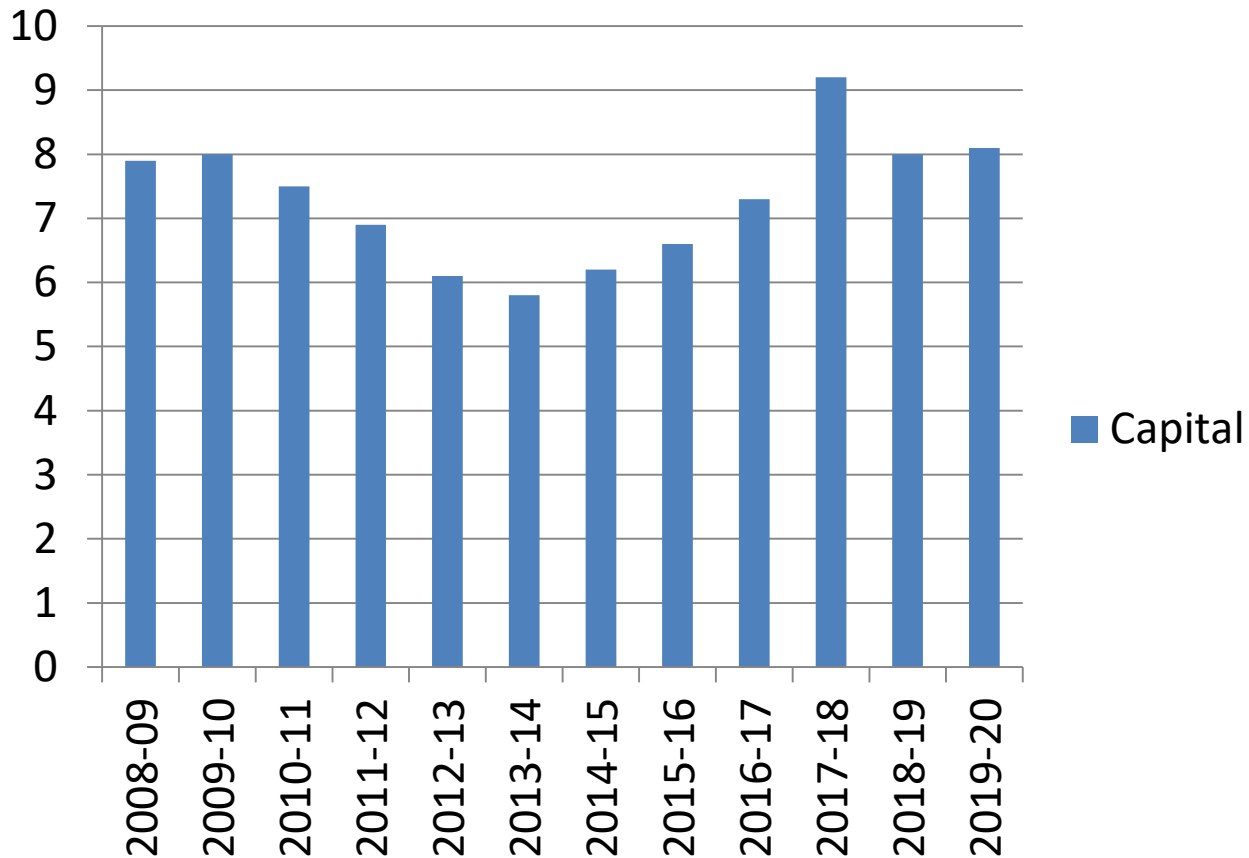
Demographics

- Alberta has a population of 4.2 million. Alberta has experienced amazing population growth prior to the downturn which has proved major challenge to governments.
- Interprovincial migration has turned negative although international migration continues strong. Natural increases remain strong.
- Population growth expected to be around 1.4 %
- BC's population is half a million larger at 4.7 million.

Capital Spending Trends

(billions)

- Alberta has consistently gone wild on capital.



Capital Spending

- Unprecedented capital spending. Alberta has always spend well above other provinces.

	2015-16	2016-17	2017-18	2018-19	2019-20
Alberta	\$6.6 b	\$7.3 b	\$9.2 b	\$8.0 b	\$8.1 b
BC	\$3.5 b	\$4.1 b	\$4.8 b	\$4.5 b	\$4.4 b
Difference	\$3.1 b	\$3.2	\$4.4 b	\$3.5 b	\$3.7 b

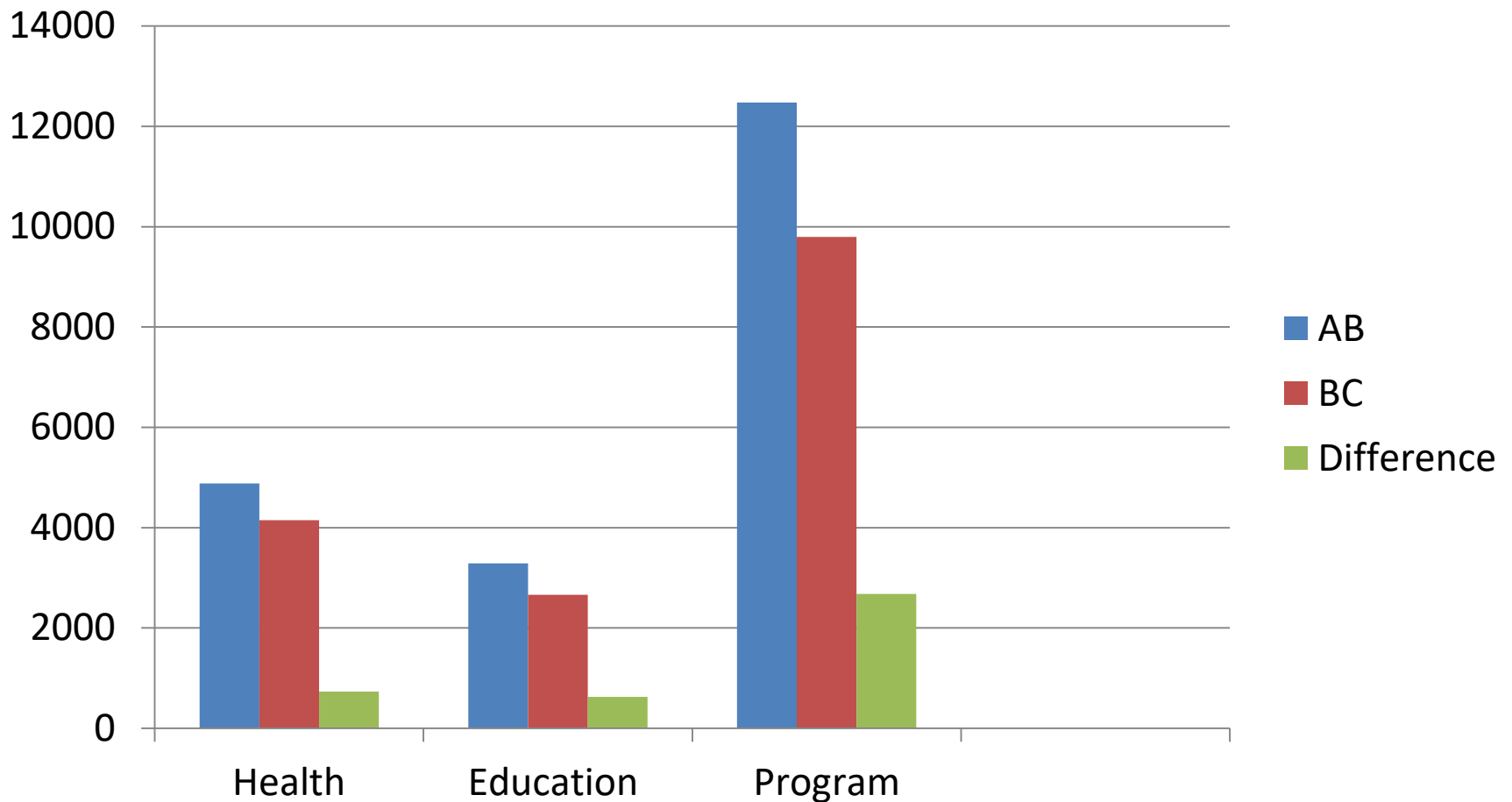
Per Capita Capital Spending

- On a per capita basis Alberta spends twice as much per person as BC.

	2015-16	2016-17	2017-18	2018-19	2019-20
Alberta	\$1,569	\$1,721	\$2,131	\$1,831	\$1,837
BC	\$737	\$868	\$999	\$923	\$893
Gap	2.1 times	2.0 times	2.1 times	2.0 times	2.1 times

Per Cap Program Spending

27% higher program spending in 2016-17



Managing Spending 2016v2015 FY

Spending up by 9.8%. Climate Plan accounted for \$1.4 billion and disaster assistance \$0.8 billion of year over year increase. Factor those out spending still increased by 5.4%

	2015-16 Actual	2016-17 Forecast	Difference
Revenue	\$42.5 billion	\$42.9 billion	\$438 million (1%)
Expense	\$48.9 billion	\$53.7 billion	\$4.8 billion (9.8%)
Deficit	6.4 billion	\$10.8 billion	\$4.4 billion

2016-17 In-Year Management

	2016-17 Budget	2016-17 Forecast	Difference
Revenue	\$40.7 billion	\$42.9 billion	\$2.2 billion (3.6%)
Expense	\$51.1 billion	\$53.7 billion	\$2.6 billion (5.1%)
Deficit	\$10.4 billion	\$10.8 billion	\$0.4 billion (3.9%)

Disaster assistance budgeted at \$200 million but ended up at \$1.4 billion. Climate leadership budgeted at \$330 million came it at \$1.4 billion. Budget had \$700 m risk adjustment.

Public Sector Pay

- Total payroll including teachers and doctors, nurses is \$26.1 billion in 2017-18 which is 55% of total operating expense.
- The 2017-18 budget includes existing collective agreements and freeze on managers.
- Assumes no increases for contracts that are coming up or in negotiation. Busy calendar includes teachers, nurses, provincial workers.

2017-18 Public Sector Pay

Estimated \$26 billion

	Amount	% of Total
AB Public Service (depts)	\$2.8 billion	10%
Other Govt Agencies	\$0.6 billion	2%
School Boards	\$6.0 billion	23%
Post-secondary institutions	\$3.5 billion	14%
Alberta Health Services	\$8.1 billion	31%
Physicians	\$5.0 billion	19%

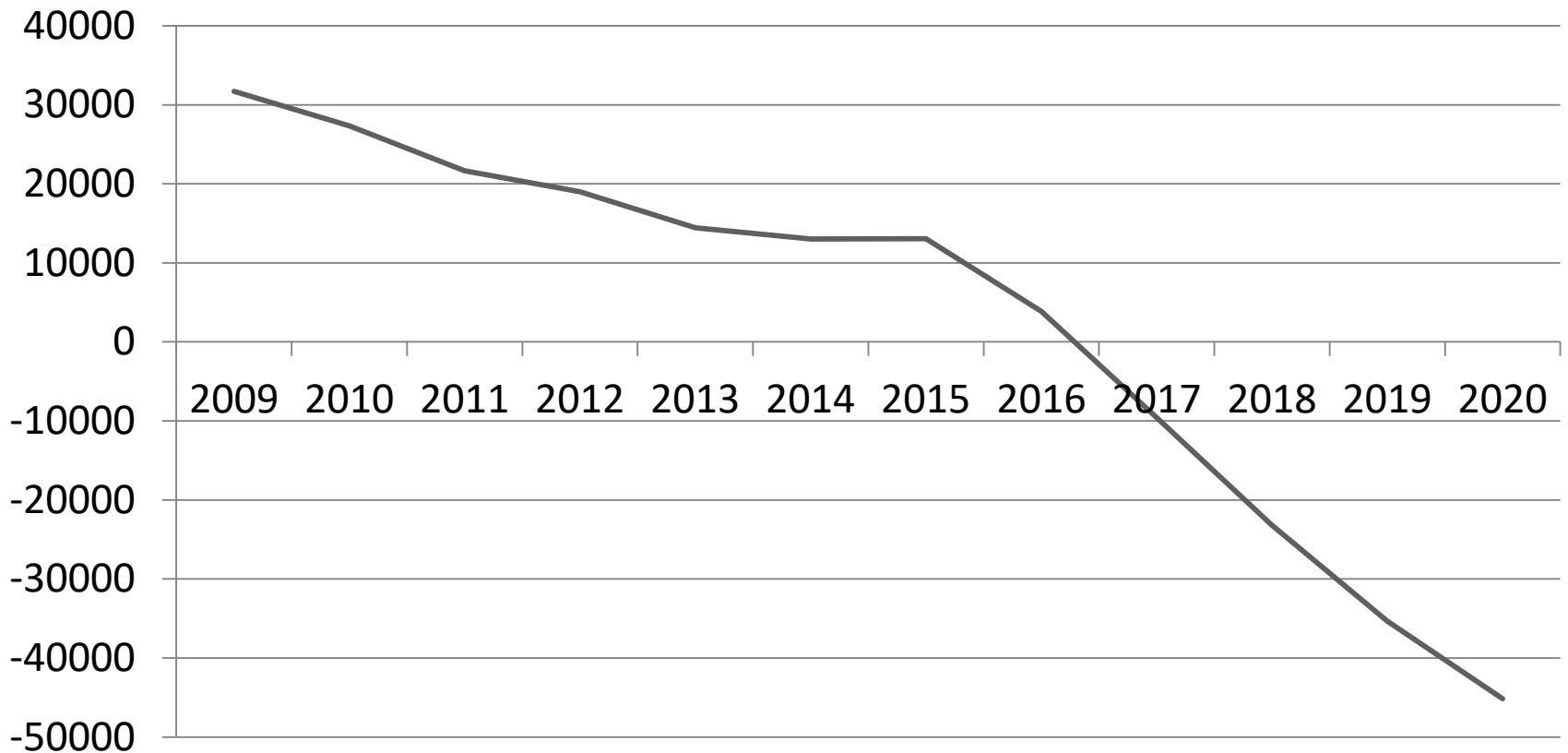
Real Deficit

- Focus on change in net financial assets. Cash deficits approach \$14 billion.

	2016-17	2017-18	2018-19	2019-20
Budget Deficit	\$10.8 b	\$10.3 b	\$9.7 b	\$7.2 b
Change Net FA	-\$13.5 b	-\$13.6 b	-\$12.1 b	-\$9.8 b

Burning through \$75 Billion

Net Financial Assets / Debt as at March 31



Rising Interest Payments

- 1994-95 dsc peaked at \$1.7 billion.
- By 2008-09 reached low of \$208 million.
- Now dsc estimated at \$1 billion in 2016-17 rising to \$2.2 billion in 2019-20.
- In 2019-20 dsc will be 5th largest ministry of government.
- **Higher debt more risk. 1 percentage point = \$230 million.**

Budget 2017 Shortcomings

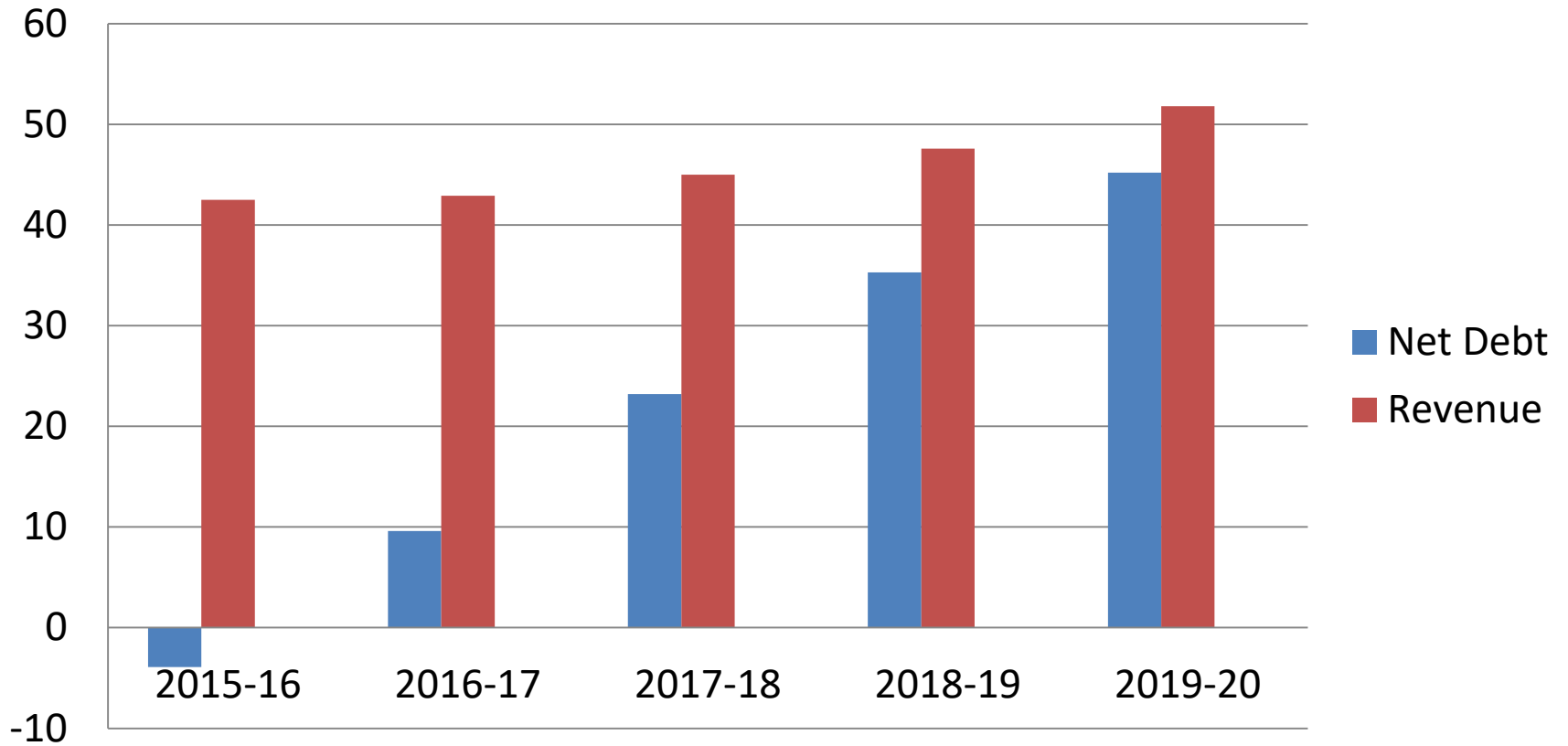
- Focus short term. No real discussion of looming m-t issues.
- Where's the balanced budget plan?
- Didn't see any reference to structural issues. No serious discussion of revenue base or bending cost curves.
- Brief mention of economic risks; no discussion of fiscal risks.

Major Risks

- Outlook for bitumen - Price, light-heavy differential, pipelines, politics (BC, fed NDP).
- Short-term thinking and domestic politics.
- Public sector wages.
- Limited policy buffers.
- Border issues with new US administration.
- Investment climate.
- Growing debt.

Net Debt vs Revenue

billions



No Fiscal Anchor

- No plan to get to a balance budget. Budget 2017 doesn't even show "fake" plan to balance the budget.
- Don't have any fiscal principles or rules to fall back on.
- What does this government stand for on fiscal issues?

Final Thoughts

- Living beyond our means. Have a quality of life we can't afford. Can't continue with spending so much higher per capita and highest wages. Need broader revenue base.
- Delaying action to begin the readjustment process guarantees future spending cuts and tax increases more severe.
- Missed opportunity to start dialogue.

Sask Budget Stark Contrast

- Balance the budget in 3 years
- Increasing pst by 1 point and widening base
- Reducing pit rates with top rate below AB
- Reducing cit rate to 11% compared to 12% in AB
- New Commercial Innovation incentive which could lower cit to 6%.
- Cutting capital from \$1.9 b to \$700 m
- Reducing psi operating funding by 5%
- Cutting 3.5% (\$250 m) from public sector comp
- Looking to cut non-core health services etc. etc.



KEEP CALM
AND
PRAY