ALBERTA BUDGET 2020

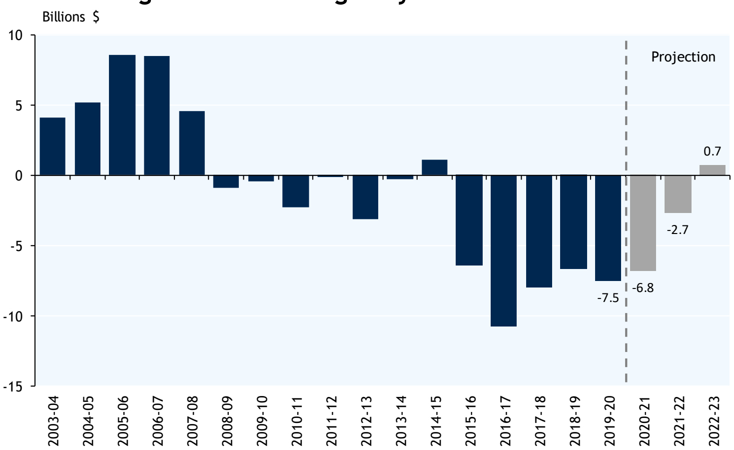
February 28, 2020

Staying the (tough) course to balance

- Budget 2020 still projects a balanced budget by FY 22/23 amid economic headwinds
- Revenues continue to hinge on resource sector
- Operating expenditures set to decline by 0.8% on average over the three year fiscal plan
- Capital plan will grow to $7 billion in FY 20/21

Things have become more challenging for Alberta since the UCP government tabled their first budget in October 2019. Oil prices are down more than 20% so far this year on coronavirus fears. Rail blockades have affected supply chains more recently – and this is after a strike in November affected shipments. Political and economic risks have raised more questions about the outlook for the oil patch. However, Alberta's Budget 2020 continues to rely heavily on the energy sector to put the provincial fiscal affairs back on its feet. In fact, resource revenues are projected to surge from $5.1 billion in FY 20/21 to $8.5 billion in FY 22/23 (a 68% increase!).

Alberta government budgetary balance



Source: Alberta Finance and Treasury Board, RBC Economics

In the main, Budget 2020 doesn't veer too much from the previous one. It's still projecting the government will balance its books by FY 22/23 by reducing spending and counting on a rebound in resource revenues. The principal addition is a "Blueprint for Jobs" – heralded in the Throne Speech earlier this week as a manifesto for supporting and diversifying Alberta's ailing labour market. The blueprint sets ambitious goals for a wide range of sectors from the primary agriculture sector, tourism industry to finance and fintech. However, Budget 2020 is short on specifics on how the government intends to achieve those goals. The overall strategy to boost jobs and the economy still largely rests on lower business tax, attracting investment in primarily the energy sector, reducing red tape, providing better skills training and building critical infrastructure.

Economic growth assumptions

	2020	2021	2022	2023
Real GDP growth (%)				
Budget 20120	2.5	2.8	2.9	2.8
RBC	1.7	2.3	-	-
Nominal GDP growth (%)				
Budget 2019	2.8	5.9	5.9	5.5
RBC	3.7	4.2	-	-

Source: Alberta Treasury Board and Finance, RBC Eonomics

Economic assumptions made by the government have a tendency to be revised downward. GDP growth for 2019 in Budget 2020 is down to 0.3% from the 0.6% expected in the previous budget. Our own estimate for Alberta's growth in 2020 is well below the 2.5% expected by the government, at 1.7% (as is the

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average of all private forecasters at 1.9%). This combined with their optimistic oil price outlook especially towards the end of the fiscal plan (the light-heavy differential is expected to hit $14.6 by FY 22/23) is reason to be cautious about the viability of the plan. The focus is very much on reducing expenses and finding efficiencies in government departments, while the revenue side is primarily hinged on an unpredictable resource. While we applaud the prudence on display in the two budgets, the timeline for balancing the budget may risk getting pushed.

Deficit to decline modestly

The government projects the deficit to decline modestly in FY 20/21 to $6.8 billion (albeit higher than the $5.9 billion expected in Budget 2019), before dropping much more significantly to $2.7 billion in FY 21/22. A small surplus of $706 million is projected in FY 22/23. The deficit for FY 19/20 is now expected to be $1.2 billion smaller than projected in Budget 2019 at $7.5 billion, primarily due to savings from unused contingency funds and a reduced provision for the winding down of crude-by-rail contracts ($1.3 billion instead of $1.5 billion previously).

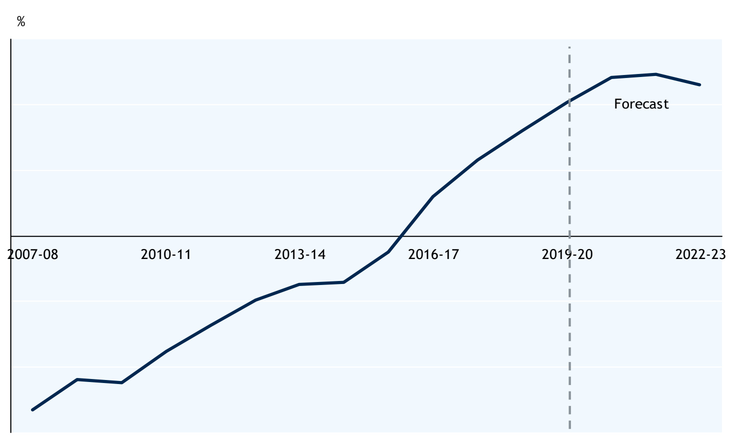
Lower revenues tied to resource sector

After rising 2.7% in FY 19/20, revenues are slated to decline by 2% in FY 20/21 owing to lower resource royalties and investment income. The last two years of the fiscal plan rely on a material bounce back in revenues largely on the assumption that increased market access to Alberta's oil and gas, and stronger energy markets will generate substantial increases in resource revenues. Between FY 20/21 and FY 22/23, resource revenues are expected to surge by 68% (from $5.1 billion in FY 20/21 to $8.5 billion in FY 22/23). Price assumptions for Western Texas Intermediate were mostly unchanged from Budget 2019 at $58 per barrel in FY 20/21, $62 per barrel in FY 21/22 and $63 per barrel in FY 22/23. Adjustments were made to the light-heavy differential – which went up to $19.10 in FY 20/21 from $18.40 expected in the previous budget. The differential will go up again in FY 21/22 to $20.60 before declining to $16.40 in FY 22/23. The government's assumptions for the differential are more cautious than private sector forecasts in the near term (FY 20/21 and FY 21/22) – however their longer term assumptions which are more material to balance the books are more optimistic. They also expect the US/CAD exchange rate to be much stronger that private sector forecasts. Assuming the sensitivities for FY 20/21 remain the same for the rest of the fiscal plan, revenues could be up to $3 billion lower in the last two years of the fiscal plan if we use RBC's assumptions for WTI, the light-heavy differential and natural gas prices. No new taxes were introduced in this budget, with several previously announced measures like the vaping tax, continued reductions to the corporate income tax and a tax on short term rentals set to come online in FY 20/21.

Support however comes from cuts to operating expenses

A central plank of Alberta's fiscal plan is spending restraint. Operating expenses are projected to decline by 0.8% on average over the three years. 15 of 21 departments will see a decline in operating expenses in FY 20/21 with the biggest cuts in advanced education, health and treasury board and finance. With the UCP government's mission to bring the cost of public goods and services to the national average over the next three years, the government intends to make cuts to the public service, implement tighter controls on public sector compensation and leave unfilled positions vacant.

Net debt to GDP



Source: Alberta Treasury Board and Finance, RBC Economics

Big boost to infrastructure spending will support job creation

Spending on infrastructure will jump 21% from $5.8 billion in FY 19/20 to $7 billion in FY 20/21. The remaining years of the fiscal plan will see declines before going back to $5.8 billion in FY 22/23. This is in line with recommendations from the Mackinnon Panel which guided the province to bring capital assets per capita in line with the rest of the provinces. A major chunk of the spending will go towards municipal support followed by maintenance of existing capital, healthcare and roads. Budget 2020 expects the plan to create 3000 jobs by 2022.

Rising debt but debt burden still low compared to other provinces

Taxpayer supported debt is set to rise 13% in FY 20/21 to $77 billion and reaching $87.8 in FY 22/23. Net financial debt to nominal GDP is set to increase from 12.1% in FY 20/21 to 12.3% in FY 21/22 before declining to 11.5% in FY 22/23. to Borrowing requirements are projected to be $10.6 billion in FY 19/20 or $4.5 billion lower than projected in Budget 2019 due to a lower deficit, closure of some regulated funds and improvements to cash management. Borrowing will increase to $15.8 billion in FY 20/21 before declining to $11.9 billion in FY 21/22 and $11.2 billion in FY 22/23.

Alberta's consolidated fiscal plan				
($ billions)	Forecast	Estimate	Target	Target
	2019/20	2020/21	2021/22	2022/23
Total revenues	50.9	50.0	54.0	58.1
Total expenditures	57.2	56.0	56.0	56.2
Program spending	41.9	40.9	44.5	48.3
Interest on public debt	9.1	9.1	9.5	9.8
Crude-by-rail provision	1.3	-	-	-
Contingency(disaster assistance)	-	0.75	0.75	0.75
Revenue forecast allowance	-	-	-	0.5
Reserve	1.3	0.8	0.8	1.3
Surplus/(Deficit)	(7.5)	(6.8)	(2.7)	0.7