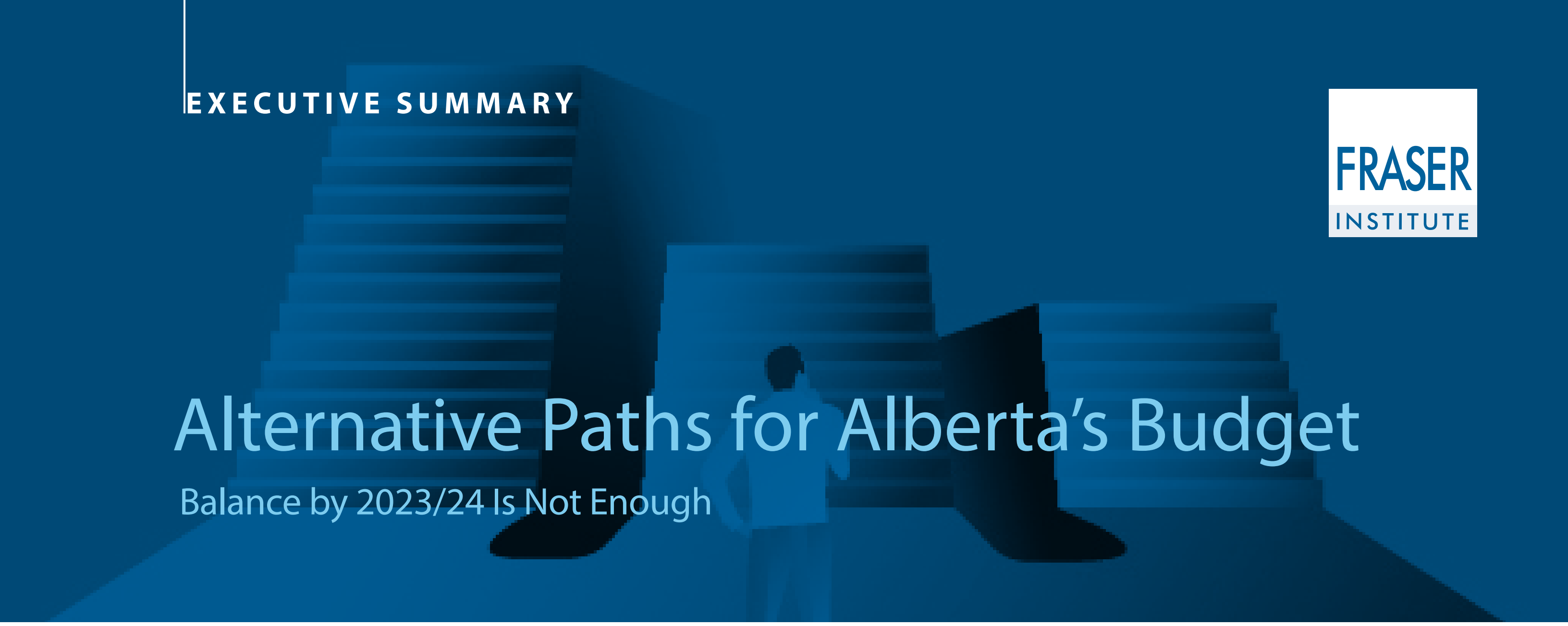
EXECUTIVE SUMMARY



Alternative Paths for Alberta's Budget

Balance by 2023/24 Is Not Enough

by Steve Lafleur and Joel Emes

Alberta faces significant fiscal and economic challenges. The government has run nearly uninterrupted deficits since 2008/09 and has seen an approximately $57 billion decline in its net financial assets between 2008/09 and 2017/18. The government has stated that it will continue to run significant budget deficits for many years before finally achieving balance in 2023/24. This unambitious target for balancing the budget is not enough for three reasons: running deficits until 2023/24 would significantly add to the province's rising debts; the current budget is based on an elevated level of taxation; and the current fiscal trajectory will mean that the provincial government will remain on the "resource roller coaster".

We use a detailed model of Alberta's finances to project the evolution of Alberta's spending levels, annual budget deficits, and debt accumulation between now and 2023/24 under various spending scenarios. First, we evaluate whether the provincial government is currently on track to meet its target date for eliminating the deficit elimination. It is not: our projection suggests that under existing trajectories for revenue and spending, the province will still have a $5 billion deficit in 2023/24. In the absence of a substantial—and unexpected—increase in revenue, our model suggests, therefore, that a significant slowdown in the rate of spending growth will be required to achieve a balanced budget by 2023/24. Specifically, we estimate that the provincial government will need to hold the growth of program spending to an average annual rate of 0.8% in the years ahead. These forecasts show that a balanced budget can be achieved by 2023/24 without nominal spending reductions. Given the scale of Alberta's fiscal challenges, this represents an unambitious objective.

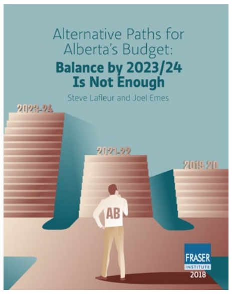
There are several reasons that running deficits for such a long time into the future will be perilous. First, continued deficits are leading to a significant accumulation of debt. Our projection shows that during the government's proposed timeline for deficit elimination, Alberta's net debt will climb to $62 billion and the cost of servicing it will double between now and 2023/24.

Second, the provincial government recently introduced several tax increases that have badly undermined the province's former tax advantage. The spending plan outlined above will leave no room to reduce the province's elevated tax burden. This is particularly important in light of recent decreases in US federal taxes. The province has gone from the lowest top statutory personal income and corporate income tax rates in North America to middle of the pack or worse in a few short years. So balancing the budget on a slow timeline without nominal spending reductions will mean foregoing an opportunity to restore the province's formerly unambiguous advantage within North America as a result its low tax rates.

Third, this plan would not allow the province to get off the "resource roller coaster". In other words, it would continue to use 100% of non-renewable resource revenue for current spending rather than contributing a portion to the Heritage Trust Fund, as was envisioned when the fund was created. Moreover, failing to get off the resource roller coaster leaves provincial finances vulnerable to future fluctuations in commodity prices.

What level of spending restraint or nominal reductions would be needed to achieve a balanced budget sooner or create fiscal room to address these? Our forecasts suggest the budget can be balanced one year ahead of schedule (by 2022/23) by holding the growth of program spending to 0.25% annually starting in 2018/19. Further, with modest annual spending reductions of 0.55% between now and 2021/22, the deficit could be eliminated two years ahead of schedule. Balance could be achieved by 2020/21 by reducing program spending at an average annual rate of 1.85% and, finally, the budget could be balanced by 2019/20 if the government were to reduce nominal program spending by 4.7% annually over the next two years.

We have not evaluated the specific advantages and disadvantages of the various deficit elimination strategies laid out above, but it is evident that balancing the budget at an earlier date would reduce the accumulation of debt while giving the provincial government room to provide tax relief and to reduce the province's reliance on revenue from non-renewable resources.



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