Scotiabank

GLOBAL ECONOMICS

FISCAL PULSE

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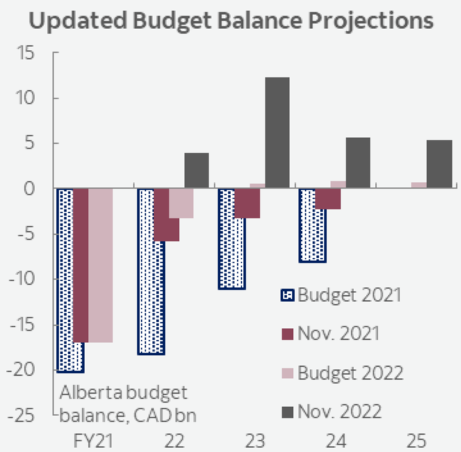
Alberta: 2022–23 Mid-Year Update

FISCAL PRUDENCE IN TIMES OF UNCERTAINTY

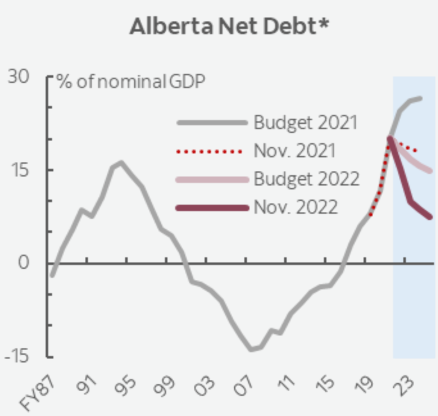
- **Budget balance forecasts: $12.3 bn (2.6% of nominal GDP) in FY23, $5.6 bn (1.2%) in FY24, $5.3 bn (1.1%) in FY25, respective improvement of $11.8 bn, $4.7 bn, and $4.6 bn versus Budget 2022 (chart 1).**
- **Net debt: revised down by an average of $23 bn each year through FY25; as a share of nominal output, net debt is now expected to decline steadily from 9.9% in FY23 to 7.5% by FY25 (chart 2).**
- **Economic forecasts: nominal GDP forecast raised from 11.2% to 24.1% for 2022 but reduced from 6.5% to 1.7% for 2023; WTI price projections lifted to US$91.5/bbl in FY23, US$78.5/bbl in FY24 and US$73.5/bbl in FY25.**
- **Borrowing requirements: $1.4 bn in FY23, $0.8 bn in FY24, $3.75 bn in FY25, representing a combined FY23–25 reduction of $11 bn from the Budget estimates.**
- **Capital spending: planned outlays are projected to total $7.6 bn in FY23 and gradually decline to $6.6 bn in FY25—a total of $785 mn increase from Budget 2022 over the three fiscal years, including the $137 mn carried forward from the previous fiscal year according to project progress.**
- **The updated fiscal plan incorporated the newly-announced affordability package with an estimated cost of $7 bn between FY23 and FY25, which will hit the economy in the coming quarters.**
- **The Update penciled in modest increases in spending profile and outlined a tentative plan to distribute surplus cash for debt repayment and savings. With the province's bottom line highly linked to oil prices assumptions, fiscal prudence and conservative planning is largely warranted in an environment of heightened uncertainty. Although the upgraded spending profile remains relatively restrained even with a sizable affordability package built in, we could expect additional spending pressure with an election around the corner next year.**

Chart 1



Sources: Scotiabank Economics, AB Treasury Board & Finance.

Chart 2



* From Finance Canada Fiscal Reference Tables.
Sources: Scotiabank Economics, Finance Canada, AB Treasury Board & Finance.

OUR TAKE

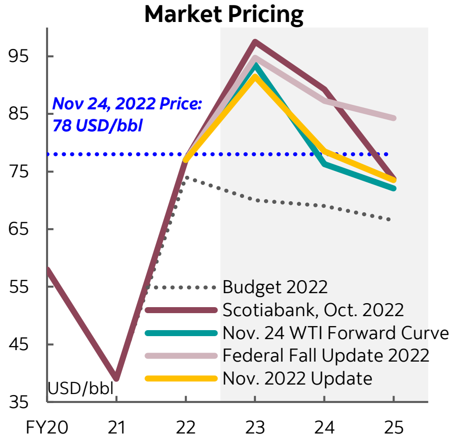
As expected, Alberta's fiscal path saw a material upgrade versus estimates in Budget 2022 back in February, mostly due to the surge in energy prices driven by geopolitical uncertainties. The province is estimating a $12.3 bn surplus for FY23, followed by two years of surpluses of over 1% of nominal output. Planning to use bulk of its cash surplus for debt repayment, the province now expects its net debt-to-GDP ratio to trend on a steep downward path and return to 2019 levels by FY25. Debt servicing costs remain largely unchanged with reduced debt projections offsetting the effect of rising interest rates.

Rising energy prices contribute to the bulk of bottom-line improvements over the planning horizon. Non-renewable resource revenue projection doubled in FY23 versus the Budget, accounting for over 40% of own-source revenue. FY24 and FY25 own-source revenue forecasts were also lifted, with almost all windfalls stemming from resource revenue gains. On the flip side, PIT projection was revised down over the planning horizon, reflecting weakened economic outlook and the indexation of the PIT brackets to inflation (discussed later in the policy section). Own-source revenue is now projected to decline over the three fiscal years, driven by falling non-renewable resource royalties.

Fiscal planning continues to err on the side of caution. The Update assumes WTI price to average US$91.5/bbl in FY23, which is equivalent to assuming an average price of $75 for the rest of the fiscal year, leaving room to cushion recent downward pressure on crude prices. Over the next two fiscal years, WTI price projections are very close to levels suggested by the current pricing of WTI futures, at US$78.5/bbl in FY24 and US$73.5/bbl in FY25. In comparison, the federal government fall update assumes WTI price to average above US$80/bbl over the next three years (chart 3). The province's fiscal situation is highly tied to oil prices and although the WTI assumptions used in the update seem relatively conservative, there could be some downside risks to the revenue outlook. As every US$1 increase in WTI could lead to $500 mn in revenues according to the Budget's estimate, to completely offset the surpluses penciled in for FY24 and FY25, WTI would need to average below US$67/bbl in FY24 and US$63/bbl in FY25.

Chart 3

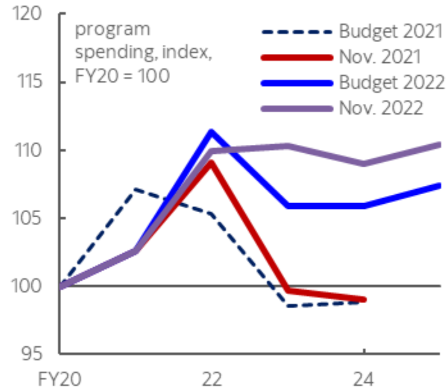
Oil Price Forecasts Close to Market Pricing



Sources: Scotiabank Economics, AB Treasury Board & Finance, Bloomberg.

Chart 4

Comparing Spending in Recent Alberta Fiscal Plans



Sources: Scotiabank Economics, AB Treasury Board & Finance.

The government is using part of the revenue windfalls to raise spending profile and provide pocketbook relief to households. Total program spending projection saw a slight upgrade versus Budget estimates, raised by $2.5 bn in FY23 and then by $1.7 bn each year in FY24 and FY25—well within the bound of revenue windfalls (chart 4). Overall program spending growth remains restrained over the projection horizon, especially considering the $2.8 bn additional affordability initiatives provision over the three years.

Bulk of new policy measures target cost of living concerns, partially offset the projected revenue gains from FY23 to FY25. Some big-ticket items in the affordability package include the already announced $600 payouts to seniors, middle-income families with dependent children and AISH and PDD receivers, as well as the extension of fuel taxes suspension and electricity rebate. Although relatively sizable with an estimated fiscal impact of $2.6 bn (0.6% of nominal GDP) in FY23 and $2.2 bn (0.5%) in FY24, the affordability measures are fairly substantive with a tilt towards lower- to middle-income households, and the majority of the impact should be short-lived. More permanent changes include indexing personal income tax brackets and income supports to inflation, which has long-term but limited fiscal impact on the province's bottom line.

Updated Fiscal Forecast

$ billions except where noted

	FY22		FY23		FY24		FY25	
	Feb. '22	Final	Feb. '22	Nov. '22	Feb. '22	Nov. '22	Feb. '22	Nov. '22
Total Revenue	**61.7**	**68.3**	**62.6**	**76.9**	**63.1**	**69.6**	**63.9**	**69.9**
Own-Source	50.4	56.7	50.6	64.4	51.5	58.0	52.0	57.6
PIT	13.3	13.3	13.4	13.3	14.4	13.8	15.5	14.7
CIT	3.3	4.7	4.0	6.3	4.5	6.2	4.9	6.6
Nat. Resources	13.2	16.2	13.8	28.1	12.3	19.2	10.9	16.0
Other	20.5	22.5	19.3	16.7	20.2	18.9	20.7	20.3
Fed. Transfers	11.3	11.6	12.1	12.5	11.6	11.5	11.9	12.3
Total Expenditure*	**61.8**	**64.4**	**61.1**	**63.9**	**61.5**	**63.2**	**62.4**	**63.8**
Programs**	59.4	61.7	58.4	61.2	58.7	60.4	59.6	61.2
Health	25.0	25.1	24.4	24.8	24.4	24.9	24.9	25.7
Education	15.1	14.3	15.4	15.4	15.4	15.4	15.5	15.6
Other	19.3	22.3	18.7	21.0	19.0	20.1	19.1	20.0
Debt Service	2.4	2.6	2.7	2.7	2.8	2.8	2.8	2.6
Contingency	**3.1**		**1.0**	**0.7**	**0.8**	**0.8**	**0.8**	**0.8**
Balance	**-3.2**	**3.9**	**0.5**	**12.3**	**0.9**	**5.6**	**0.7**	**5.3**
% of GDP	*-0.9*	*1.1*	*0.1*	*2.6*	*0.2*	*1.2*	*0.2*	*1.1*
Net Debt	**64.0**	**57.0**	**65.1**	**46.0**	**64.7**	**41.2**	**63.9**	**36.1**
% of GDP	*18.3*	*15.2*	*16.7*	*9.9*	*15.6*	*8.7*	*14.8*	*7.5*
Debt Service								
% of Revenue	*3.9*	*3.9*	*4.3*	*3.5*	*4.4*	*4.0*	*4.4*	*3.7*

* Net of contingency. ** Net of pension provisions.
Sources: Scotiabank Economics, AB Treasury Board & Finance.

The Update outlined a tentative plan to allocate 70–75% of surplus cash to repay taxpayer-supported debt and invest the rest. That means $13.3 bn cash will go into debt repayment in FY23, followed by $2.3 bn in FY24 and $1.4 in FY25. However, this could change as the year unfolds as the government continues to evaluate the trade-offs between debt reduction and increasing savings in an environment of high inflation.

FY23–25 borrowing requirement projections were revised significantly lower than anticipated at Budget time. Due to abundant surplus cash, the province eliminated this year's planned $2.2 bn government borrowing all together, with the remaining $1.4 bn borrowing requirements dedicated to provincial corporations and GBEs. The borrowing program is now forecast at $825 mn in FY24 and $3.75 bn in FY25.