# Alberta

## 2013-2014 Budget Preview

As a think tank dedicated to improving the long-term prosperity of western Canada, the Canada West Foundation is paying close attention to the signals being sent by the region's provincial governments and the federal government in their 2013/14 budgets.

Western Canada is facing a number of challenges that governments must address including sluggish productivity growth, looming labour shortages, gaining access to new markets and enhancing the performance of the public sector. We need to be investing in the future, not just spending in the present.

Alberta will be the second of the western provinces to release its 2013/14 fiscal plan, with its budget to be tabled on March 7.

With the above challenges in mind, there are five things we hope to see in Thursday's budget:

1) Measures to reduce the use of resource revenue to fund current spending.

2) New investments in the Heritage Fund.

3) Initiatives to address future labour shortages.

4) Steps to improve value for money in critical government services like health and education.

5) Openness to changing the future tax mix in Alberta.

Our post-budget analysis—available on March 8, 2013—will assess the degree to which the budget addresses these issues.

## 1

## Reducing Volatility: Treating non-renewable resources differently

Alberta's current fiscal shortfall is the result of a "bitumen bubble"—a wider-than-normal gap between the prices Alberta producers receive for their heavy oil and North American benchmark prices. This price gap is the most recent manifestation of the broader problem facing the Alberta government—its reliance on volatile non-renewable resource revenues to fund current spending.

About 30% of the province's budget comes from oil and gas revenues which, as recent history has shown, can fluctuate dramatically from one year to the next. Past experience also demonstrates that it is impossible to make long-term strategic plans for building a prosperous economy when faced with a highly inconsistent revenue stream.

The long-term solution to this problem is to reduce or eliminate dependence on resource revenues to fund heath care, education and other current expenditures.

**The Canada West Foundation hopes that the budget will begin the process of reducing the reliance on non-renewable resource revenues to finance current spending.**

## 2

## Saving for the Future: A Plan to rebuild the Heritage Fund

As noted above, Alberta relies on revenues from the one-time sale of unpredictably-priced, non-renewable assets to finance current spending. While this provides obvious benefits to current Albertans, it does not plan ahead for the future.

Alberta needs to rebuild its Heritage Fund to ensure that future generations benefit from its resource wealth. While the province may not run out of oil anytime soon, the long-term future of petroleum extraction is far from certain. Low oil prices, a lack of pipeline access to tidewater, improvements in fuel efficiency and the rise of alternative energies could all undercut future demand for petroleum. The province may never get the chance to run out of oil.

**In the 2013 Budget, the Canada West Foundation hopes to see a long-term plan to rebuild the Heritage Fund. Ideally, *all* non-renewable resource revenues would eventually be committed to the Heritage Fund to build a revenue stream for future generations.**

## 3

## Anticipating Tomorrow's Needs: Acting now to address potential labour shortages

A combination of economic growth, investment in the oil and gas sector, and demographic changes is pointing to future labour shortages in Alberta. Alberta has experienced such shortages in the past, but those were the result of investment and construction booms that temporarily strained labour market capacity. By contrast, future labour shortages are expected to be in permanent, full-time positions, largely in engineering and skilled trades. Recent forecasts suggest that the oil and gas industry will need close to 10,000 new permanent workers over the next two years alone.

At the same time, however, an aging population is expected to result in a significant withdrawal of experienced workers from the labour force at a time when their skills are needed most. In response, the provincial government has looked to increase the size of the labour pool by recruiting Canadians from other provinces as well as immigrants and temporary workers from the US and other countries.

A lack of skilled labour would not only slow economic growth in the province, but would also create inflation and raise costs for all Albertans. Moreover, neighbouring provinces have identified similar concerns about their workforces, meaning that, in future, there may not be a significant pool of out-of-province workers to draw upon.

**In the 2013 Budget, the Canada West Foundation hopes to see measures designed to address future labour shortages and skills training requirements in Alberta.**

## 4

## Getting Full Value for Money: Improving government performance

Albertans are accustomed to relatively high levels of government spending at comparatively low levels of taxation. Only in Newfoundland and Labrador and Manitoba is per capita government spending higher than in Alberta. Nowhere is the overall tax burden lower.

However, the fact that the Alberta government spends generously on its residents does not mean that Albertans are always getting value for that money or receiving the best-quality government services. For example, Alberta spends more per person on health care than almost any other province (in spite of a much younger-than-average population), but is not achieving significantly better health outcomes than other jurisdictions.

**The Canada West Foundation believes that outcome-based performance measures and the study of best practices in other jurisdictions would help the Alberta government ensure that its residents are receiving full value for their money. It hopes to see steps taken to this effect in the 2013 Budget.**

## 5

## Changing the Revenue Mix: Considering a sales tax

One way for the provincial government to reduce its dependence on non-renewable resource revenue is to introduce a sales tax. A sales tax is economically efficient and provides a consistent and reliable source of revenue for the provincial government. It would reduce year-over-year volatility in government revenues while also providing the fiscal room to allow Alberta to begin reinvesting resource revenues into the Heritage Fund. Sales tax revenue could also be used to finance income tax cuts.

There are many questions surrounding how a sales tax would be introduced in Alberta. Would it be harmonized with the GST? How large would it be? Would it be temporary or permanent? Would it affect Alberta's economic competitiveness? What steps would be needed to make the tax progressive? Perhaps most important, could future governments resist the temptation to spend this new income instead of using it to create the fiscal room to reduce dependence on resource revenues?

It is too early to expect the Alberta government to introduce a sales tax in the 2013 budget. The government would have to convince Albertans of the benefit of a sales tax and to provide adequate notice and opportunities for public consultation. Nevertheless, a sales tax is an important piece of the puzzle in moving Alberta to a more sustainable fiscal footing.

**In the 2013 budget, the Canada West Foundation hopes to see a commitment to reforming the tax mix in Alberta.**

## 2012 Budget Review

Alberta's 2012 budget was a pre-election document that set the province on a path to eliminate the deficit in two years. The provincial economy was doing well at the time. Oil prices were high and revenues from non-renewable resources were strong. A year earlier, the province had projected a deficit of $3.4 billion in 2011/12. By the time the 2012 budget came out, the deficit was expected to be in the range of $1.3 billion. The budget projected a deficit of $886 million for 2012/13 (not including $2.2 billion in off-budget capital spending) and a target surplus of $952 in 2013/2014.

The government's plan was for continued strength in the Alberta economy and resource revenues to grow the province out of deficit. Based on somewhat optimistic assumptions about the Alberta economy, it projected revenue growth of 4.6% in 2012/13, followed by increases of 9.3% next year and 11.5% the year after. For 2012/13, the province assumed that resource revenues would be essentially unchanged compared to the previous year; most of the projected revenue growth was to come from higher personal and corporate income tax revenue. For the following two years, however, Alberta was counting on extraordinary growth in non-renewable resource revenues. It projected increases of more than 19% per year in 2013/14 and in 2014/15.

On the expenditure side, the Alberta budget called for program spending increases of 3.3% in 2012/13, focusing on three broad priorities: families and communities, securing Alberta's economic future, and advancing world-leading resource stewardship. Health and wellness spending—already the largest expenditure category by far—was budgeted to increase by 5.1%.

## 2012-2013 Fiscal Update

A few months after the budget was released, the Alberta government received some good news: because of higher-than-expected land sales, investment income and oil prices in the first three months of 2012, the province had nearly succeeded in balancing its budget three years early. Instead of an estimated $1.3 billion, the 2012/13 budget deficit came in at just $23 million. However, the fiscal situation deteriorated shortly thereafter.

In November 2012, Alberta released its fiscal update for the first half of the current budget year (April-September). Deficit projections for 2012/13 were revised from $886 million to between $2.3 and $3.0 billion. Three months later, in its third quarter update, the province lowered expectations even further; the deficit is now expected to be between $3.5 and $4.0 billion.

The fiscal shortfall is entirely the result of lower-than-expected resource revenues. Government spending has been right on budget and income taxes have produced significantly more revenues than initially forecast. However, the government overestimated crude oil and natural gas prices and underestimated the size of the crude oil price differential between western Canadian heavy oil and North American benchmark prices. The result is a $2.4-billion revenue shortfall through the first nine months of the 2012/13 fiscal year.

This budget preview was prepared by Canada West Foundation Senior Economist Michael Holden. The opinions expressed in this report are those of the author and are not necessarily those of the Canada West Foundation's Board of Directors, funders or advisors.



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