

Alberta Fiscal 2017–18: Q3 Update

THE RED INK BEGINS TO RECEDE

- Alberta announces strong economic growth for calendar 2017 and a revised deficit of \$9.1 billion for fiscal 2017–18 (FY18) that is decisively narrower than the *Budget* estimate of \$10.5 billion.

REVENUE DETAILS

The \$1.4 billion narrowing of the FY18 deficit mirrors, relative to *Budget*, revisions that raise revenues \$1.96 billion and remove the \$0.5 billion risk adjustment, and this more than covers the \$1.03 billion increase in expenditures.

A robust 10.8% jump in FY18 revenues is projected as of Q3, propelled by stronger investment income and resource receipts and an improvement in the Balancing Pool calculated liability. The in-year increase in investment income is almost 40% to \$3.1 billion.

Alberta's underlying assumptions of economic growth are now quite buoyant. Rising energy and manufacturing exports plus an upswing in consumer spending are expected to have lifted provincial real GDP by 4.5% in calendar 2017. In calendar 2018, as production ramps up at several large oil sands plants, real GDP is assumed to climb a further 2.8%.

Taxes are the only key revenue lower than Budget, with FY18 growth trimmed to 5.1% from the initial 7.8% estimate. With reduced 2016 assessments, \$0.3 billion from FY18 personal income tax receipts are decreased by \$0.3 billion, resulting in growth of just 0.9% for this fiscal year.

Resource receipts are now expected to be \$0.8 billion higher at \$4.5 billion, a sizeable gain from the FY16 low of \$2.8 billion though still a fraction of the FY07 peak of \$12.3 billion. Land lease sales revenues are expected to be \$0.4 billion larger and lower producer costs are enabling a \$0.5 billion in-year increase on crude oil plus natural gas and by-products royalties.

The negative impact of the lack of tidewater access for Alberta oil is discussed with several metrics. Alberta reports that oil sands production since 2014 has climbed by over 500,000 barrels per day (bpd) and a further 300,000 bpd are anticipated by the end of 2018. With existing pipelines fully utilized*, rail unable to fill the gap and rising oil output, unexpected events requiring a capacity buffer are causing market volatility and steeper heavy oil discounts. Bitumen royalties for FY18 are now expected to be \$188 million below *Budget* because of wider discounts in recent months after unexpectedly low discounts in early FY18. For *Budget 2017*, Alberta estimated that gaining tidewater access would allow oil producers' returns to climb by up to \$7/barrel. As well, the government estimates that the additional producer revenues from smaller discounts and reduced transportation uncertainty would raise the capital spending plans from 2018 to 2022 by \$10 billion, and boost royalties by \$9 billion.

CONTACTS

Mary Webb
416.866.4202
Scotiabank Economics
mary.webb@scotiabank.com

Alberta's Balance Sheet Summary as of March 31, \$ billions except where noted

	FY17	FY18	
	Final	Budget	Q3
Heritage Fund & Endowment Funds	19.8	20.2	20.3
Contingency Account	2.3	0	0.04
Other Financial Assets	44.2	43.7	47.6
Financial Assets	66.3	63.9	68.0
Liabilities for Capital Projects	23.8	29.8	29.3
Debt: Pre-1992 Teachers' Pension Plan	0.9	0.9	0.9
Direct Borrowing for <i>Fiscal Plan</i>	8.6	15.1	11.5
Pension Liabilities	10.0	9.8	9.7
Other Liabilities	31.9	31.0	36.8
Total Liabilities	75.2	86.5	88.2
Net Financial Assets	-8.9	-22.6	-20.3
% of GDP	-2.8	-6.7	-6.0

Source: Alberta Finance; nominal GDP forecast: Scotiabank Economics.

* The three major pipeline projects are: the Line 3 Replacement (+370,000 bpd); the Trans Mountain Expansion (+590,000 bpd) and the Keystone XL pipeline (+830,000 bpd).

EXPENDITURE DETAILS

Program spending growth for FY18 rises to 7.8% from the *Budget* estimate of 2.8%. Though the \$200 million of targeted in-year saving is accomplished and the Province reports efficiencies in health care and from the consolidation of common department operating expenses, operating expenditures are still almost \$0.5 billion ahead of *Budget* reflecting cost pressures in areas such as income support. Several expenditure areas are lower, including decreases in the debt service and pension provisions (table, p.2).

The Capital Plan, reported to be \$0.9 billion less than the \$9.2 billion *Budget* estimate in Q2, is now expected to match *Budget* with shortfalls due to savings and re-profiling projects roughly offset by moving municipal grants forward, including some of the funding under the *Climate Leadership Plan*. Municipal Affairs' capital outlays are raised by \$0.8 billion to \$2½ billion for FY18.

THE BALANCE SHEET AND BORROWING

Financial assets are expected to climb \$1.7 billion during FY18, ending the year \$4.0 billion ahead of *Budget*. Driving the increase is the Province's addition of a \$5.0 billion cash reserve for risk management, a precaution positively regarded by the rating agencies for several other Provinces. Other asset increases include \$0.5 billion for the Heritage Fund and endowment funds from inflation-proofing and net income retention.

Liabilities by March 2018 are expected to be \$13.0 billion above a year earlier, and \$1.7 billion ahead of *Budget*. Of note, however, is the decrease in Direct Borrowing for the Fiscal Plan.

OUTLOOK

Alberta is benefitting from a robust first-year economic recovery in calendar 2017, with a substantial benefit for the FY18 budget bottom line. However, the Province's fiscal repair efforts, such as carefully managing its civil service payroll and seeking spending efficiencies, are necessary to supplement the role of growth in reducing the deficit.

Alberta's Consolidated Budget Arithmetic

\$ billions except where noted

	FY17	FY18	
	Final	Budget	Q3
Personal Income Tax	10,763	11,177	10,855
Corporate Income Tax	3,769	3,918	3,852
Carbon Levy	250	1,038	1,012
Other Taxes	5,399	5,629	5,492
Total Tax Revenues	20,181	21,762	21,211
Non-Renewable Resource Revenue	3,097	3,754	4,534
Investment Income	3,701	2,193	3,061
Other Own-Source Revenue ¹	7,335	9,221	10,157
Total Own-Source Revenue	34,314	36,930	38,963
Federal Transfers	7,979	7,988	7,918
Total Revenue	42,293	44,918	46,881
Operating Expense(net of in-year savings)	44,661	45,906	46,370
Disaster Assistance ²	1,191	235	495
Capital Grants	2,159	3,302	3,729
<i>Climate Leadership Plan : Operating Exp.³</i>	1,379	868	577
<i>Capital Grants</i>	2	68	391
Pension Provisions	-543	-237	-332
Amortization, Inventory Ch., Other	3,210	3,375	3,362
Program Spending	52,059	53,517	54,592
General Debt Service	438	619	594
Capital Plan Debt Service	580	779	761
Total Debt Service	1,018	1,398	1,355
Total Expenditure	53,077	54,915	55,947
Risk Adjustment	0	500	0
Consolidated Balance	-10,784	-10,497	-9,066
Total Capital Plan with SUCH Sector	6,578	9,175	9,165
Financing Requirements	18,311	19,795	22,733
Annual Change, %			
Tax Revenue	-2.6	7.8	5.1
Non-Renewable Resource Revenue	11.0	21.2	46.4
Total Own-Source Revenue⁴	n.a.	7.6	13.5
Federal Transfers	11.7	0.1	-0.8
Total Revenue⁴	n.a.	6.2	10.8
Program Spending ⁴	n.a.	2.8	4.9
Total Expenditure⁴	n.a.	3.5	5.4
Memo Items, %			
Own-Source Revenue / GDP	10.9	10.9	11.5
Program Spending / GDP	16.5	15.8	16.1
Consolidated Balance / GDP	-3.4	-3.1	-2.7
Debt Service / Revenue	2.4	3.1	2.9
Resource Prices: WTI Oil, US\$/bbl	47.93	55.0	54.0
Western Canadian Select, C\$/bbl	44.67	51.3	50.4
Oil Production, Bitumen, 000s bbl / day	2,549	2,906	2,855
Conventional, 000s bbl / day	431	416	449
Natural Gas, AB Reference Price,C\$/GJ	2.01	2.90	1.90
Canadian Dollar, US¢/C\$	76.2	76.0	78.0

¹ Includes the *Balancing Pool*. ² Includes Wood Buffalo wildfires. ³ Includes the present value of the FY18–FY31 coal phase-out transition payments. ⁴ Revenues & expenditures adjusted as of FY17 for change in accounting treatment of drug cost rebates. Sources: Alberta Finance; Statistics Canada; nominal GDP forecasts: Scotiabank Economics.

This report has been prepared by Scotiabank Economics as a resource for the clients of Scotiabank. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Scotiabank nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

These reports are provided to you for informational purposes only. This report is not, and is not construed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap or trading strategy involving a swap or any other transaction. The information contained in this report is not intended to be, and does not constitute, a recommendation of a swap or trading strategy involving a swap within the meaning of U.S. Commodity Futures Trading Commission Regulation 23.434 and Appendix A thereto. This material is not intended to be individually tailored to your needs or characteristics and should not be viewed as a "call to action" or suggestion that you enter into a swap or trading strategy involving a swap or any other transaction. Scotiabank may engage in transactions in a manner inconsistent with the views discussed this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

Scotiabank, its affiliates and any of their respective officers, directors and employees may from time to time take positions in currencies, act as managers, co-managers or underwriters of a public offering or act as principals or agents, deal in, own or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to securities or related derivatives. As a result of these actions, Scotiabank may receive remuneration. All Scotiabank products and services are subject to the terms of applicable agreements and local regulations. Officers, directors and employees of Scotiabank and its affiliates may serve as directors of corporations.

Any securities discussed in this report may not be suitable for all investors. Scotiabank recommends that investors independently evaluate any issuer and security discussed in this report, and consult with any advisors they deem necessary prior to making any investment.

This report and all information, opinions and conclusions contained in it are protected by copyright. This information may not be reproduced without the prior express written consent of Scotiabank.

™ Trademark of The Bank of Nova Scotia. Used under license, where applicable.

Scotiabank, together with "Global Banking and Markets", is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including, Scotiabanc Inc.; Citadel Hill Advisors L.L.C.; The Bank of Nova Scotia Trust Company of New York; Scotiabank Europe plc; Scotiabank (Ireland) Limited; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Scotia Inverlat Casa de Bolsa S.A. de C.V., Scotia Inverlat Derivados S.A. de C.V. – all members of the Scotiabank group and authorized users of the Scotiabank mark. The Bank of Nova Scotia is incorporated in Canada with limited liability and is authorised and regulated by the Office of the Superintendent of Financial Institutions Canada. The Bank of Nova Scotia is authorised by the UK Prudential Regulation Authority and is subject to regulation by the UK Financial Conduct Authority and limited regulation by the UK Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia's regulation by the UK Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorised by the UK Prudential Regulation Authority and regulated by the UK Financial Conduct Authority and the UK Prudential Regulation Authority.

Scotiabank Inverlat, S.A., Scotia Inverlat Casa de Bolsa, S.A. de C.V., and Scotia Derivados, S.A. de C.V., are each authorized and regulated by the Mexican financial authorities.

Not all products and services are offered in all jurisdictions. Services described are available in jurisdictions where permitted by law.