Alberta 2018 Budget - What's in it For Energy?

March 26, 2018

On March 22, 2018, Minister of Finance, Joe Ceci, presented the Government of Alberta's budget 2018 entitled, "A Recovery Built to Last" ("Budget 2018"). Budget 2018 includes the government's fiscal and capital plans along with economic outlook for the province moving forward. Budget 2018 follows last year's budget "Working to Make Life Better" released on March 16, 2017.

Joe Ceci stated that after the worst recession in a generation, things are "looking up" for Albertans, citing provincial job growth, a declining deficit and the fastest growing provincial economy in Canada.

Budget 2018 is focused on three pillars:

1. Diversification of the economy through certain initiatives and growing market access, as set out in more detail below;
2. No budget cuts to current public services; and
3. Projecting a balanced budget by 2023-2024.

HIGHLIGHTS OF BUDGET 2018

Provincial revenue is projected to reach $47.9 billion in 2018-2019, or 2.1% more than the 2017-2018 forecast. In light of the projected $56.2 billion in total expenses the province's current deficit sits at $8.8 billion, with a forecast that it will fall to $7.9 billion, then $7 billion, down to $4.3 billion, then $4.1 billion and finally to a $700 million surplus by spring 2024.

Notably, while Budget 2018 promises a return to balance by 2023-2024, Alberta will have a forecasted $54.2 billion in debt by the end of the fiscal year and $96 billion in total debt by 2023-2024 - an increase of approximately 638% from this government's first budget in 2015.

Highlights of Budget 2018 include:

- Bitumen royalties are expected to fall to $1.8 billion in 2018-2019 after spiking up to $2.4 billion this fiscal year;

- Crude oil royalties are expected to continue to rise and hit $1 billion, with the government predicting that the benchmark West Texas Intermediate crude oil price will average USD $59/barrel this year;
- The take from income taxes is projected to rise, with $11.4 billion from personal income tax and $4.6 billion from corporations;
- Cannabis revenue is a factor considered in the balance sheet for the first time, with Alberta expecting to generate $26 million in taxes from recreational marijuana use;
- Education spending will rise from $7.8 billion to $8.4 billion;
- Advanced education spending will rise from $5.5 billion to $6.1 billion;
- Over the next 3 years, $5.3 billion will be spent on climate initiatives from transit projects to home efficiency programs.

BUDGET 2018: IMPLICATIONS FOR THE ENERGY SECTOR

Budget 2018 reflects a "prudent" energy outlook - noting a more balanced oil market that is expected to support prices. West Texas Intermediate is expected to average USD $59/barrel in 2018-2019, $60 in 2019-2020 and $63 in 2020-2021. However, the economic and energy price assumptions relied upon in Budget 2018 are heavily predicated upon Alberta achieving increased market access, which for reasons to follow, may or may not occur.

Notable Energy and Economic Assumptions

Pipeline bottlenecks and the increasing reliance on rail are lifting transportation costs for Alberta heavy crude oil, which is once again trading at a large discount to global prices. Lack of market access is hurting heavy oil producers, government revenues and the Canadian economy in general.

Two pipeline projects approved by the federal government, The TransMountain Pipeline Expansion and the Enbridge Line 3 Expansion, would add almost one million barrels per day of crude transportation capacity by 2021, alleviating pipeline bottlenecks that are causing major headaches for the industry, affecting profitability and increasing the industry's reliance on rail. Keystone XL will also provide additional longer-term access.

Increased market access will allow for Canadian oil to reach markets where heavy oil attracts the highest prices, reducing the discount on Alberta bitumen prices relative to global prices. The TransMountain Pipeline Expansion is critical in this respect, as it would allow producers to sell into the lucrative Pacific market. Keystone XL would provide additional access to the US Gulf Coast, a key market for Alberta's heavy crude.

Budget 2018 suggests that additional pipeline capacity would lift capital invested by an estimated $10 billion and production capacity by 190,000 barrels per day between 2018 and 2023, compared to a non-pipeline access scenario.

These additional pipelines are predicted to boost Alberta's real GDP by 1.5-2% by 2023, with higher production yielding a boost in resource royalties by up to $10.5 billion between 2018 and 2023.

The concern with these assumptions is that resistance to pipeline expansion is a real threat, involving political, social and environmental roadblocks that could further delay and even stall pipeline expansion and operation entirely.

Diversification within the Energy Sector

While Budget 2018 is predicated on the assumption that pipeline capacity will increase, an additional implication of Budget 2018 is a focus on diversification within Alberta's domestic energy sector through the implementation of *Bill 1: The Energy Diversification Act.*

The *Energy Diversification Act* proposes to commit up to $2 billion to leverage private investment, including:

1. $500 million in royalty credits for a second round of the Petrochemicals Diversification Program;
2. $500 million in loan guarantees and grants to establish a Petrochemical Feedstock Infrastructure Program; and
3. $1 billion in loan guarantees and grants to initiate a Partial Upgrading Program.

The government of Alberta suggests that these three initiatives are expected to attract $10 billion in private investment, support 8000 construction jobs and hundreds more operational jobs.

TAXES

Carbon Tax Plan

Currently, there is a $30 per tonne tax on carbon. All of this revenue is now spent on rebates and emission-reduction programs. When the provincial tax reaches $40 per tonne in 2021, Budget 2018 sets out that the government still intends to use $30 per tonne for projects that are intended to reduce the carbon footprint, with the surplus going to general operating expenses. This is predicted to translate into an additional $1 billion per year being pumped into general revenues by 2023-2024.

General Tax Plan

Highlights of Budget 2018 tax plan include:

- A new interactive digital media tax credit, worth 25% of eligible labour costs;
- An extension of the Alberta investor tax credit and capital investment tax credit to 2021-2022;
- Indexation of the personal income tax system;
- No education property taxes increase; and
- Confirmation of the tax revenue collection mechanism for cannabis.

Budget 2018 does not include any cuts to personal or business taxes. It makes note that Albertans have no sales tax, no health premium and no payroll tax. The government suggests that Alberta's current tax advantage is at least $11.2 billion per year compared with any other province.

GENERAL COMMENTS ON BUDGET 2018

Budget 2018, "A Recovery Built to Last" forecasts a year-after-year reduction in the deficit with a $700-million surplus predicted by 2023-2024. However, this plan is largely predicated on the assumption that Alberta will achieve increased market access (and resulting revenue) through the operation of three pipelines (Enbridge Line 3, The TransMountain Expansion and the Keystone XL pipeline). The assumption on increased market access ought to be tempered to some degree based on uncertainty of achieving it. The TransMountain Pipeline Expansion from Edmonton to Burnaby, BC, for example, is currently facing legal challenges from First Nations and environmental groups, not to mention opposition from B.C.'s government. TransMountain is a palpable reminder of uncertainties inherent with pipeline projects and marks a potential harbinger for things to come.

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