

Establishing Policy to Respond to Economic Highs and Lows

RECOMMENDATION(S):

That the Executive Committee recommends that Council:

1. Direct Administration to complete an assessment of the built-in capacity of existing reserves to support the countercyclical fiscal policy options in Attachment 2 by 2023 Q4.
2. Direct Administration to use the assessment of existing capacity to develop formal Administration procedure or policy (including appropriate triggers) to moderate the impact of economic highs and lows.

HIGHLIGHTS

- Calgary has a highly cyclical economy that has experienced more frequent economic highs and lows than any other Canadian city with a population of one million or more over the last 15 years.
- Countercyclical fiscal policy tools adjust government revenue and spending to moderate the adverse impacts of economic highs and lows.
- This report evaluates the options for The City of Calgary, including:
 - range of available policy tools, the criteria for ranking them, and the order of preference
 - constraints associated with the policy tools as well as the opportunities the tools afford
 - costs and benefits of using these tools
 - best practices for applying these tools
- **What does this mean to Calgarians?** Calgarians will benefit from assurances that the municipal government has some tools to moderate future economic volatility and has set up a framework for deploying them promptly.
- **Why does it matter?** Although some argue that the self-corrective power of the economy should prevail, there is evidence that moderating and augmenting the level of demand for goods and services is preferred. It would help ensure that The City is better prepared to support the local economy and will offer more economic certainty to residents and businesses.
- City Council, through the Financial Task Force Implementation program (Administrative Action 32a), directed Administration to prepare a report detailing the options available to The City and identify optimal countercyclical policies. This report is a response to that direction.
 - Strategic Alignment to Council's Citizen Priorities: A well-run city
 - Background and Previous Council Direction is included as Attachment 1.

DISCUSSION

Calgary is susceptible to more frequent economic highs and lows. It makes countercyclical policies vital. These policies work opposite to the trend of the business cycle and smooth out variations in economic activity over time.

The primary purpose during downturns is to stimulate demand for goods and services to boost the economy, provide relief for those most impacted by an economic downturn, and prevent the loss of some productive capacity in the economy. The goal during unusually high upturns is to moderate demand for goods and services to avoid high inflation, avoid discouraging or crowding out private sector spending, and reduce production activity from unsustainably high levels.

Establishing Policy to Respond to Economic Highs and Lows

The range of tools available to address this issue is narrowest for municipalities. Countercyclical fiscal policy tools adjust government revenue and spending. Specifically, government spending should be higher, and revenue should be lower during downturns. Conversely, government spending should be lower, and revenue should be higher for unusually high upturns. However, municipal finance may have difficulties being countercyclical due to budget limitations and fiscal constraints of this level of government.

The detailed investigation into the countercyclical fiscal policy actions available to The City is available in Attachment 2, which covers:

The range of policy actions, the criteria for ranking them, and the resulting order of preference

The analysis identified five policy tools for The City of Calgary. The analysis also extended to developing a set of criteria for evaluating their suitability. The criteria are:

- Cost effectiveness
- Timeliness of impact
- Stimulus effect

Using these criteria, Administration developed a ranking of the five policy tools. In the context of applying these tools to address an economic downturn, the order of preference is as follows:

- (1.) *Temporarily Increase Operating Expenditures*
- (2.) *Accelerate Capital Expenditures*
- (3.) *Targeted Business Relief*
- (4.) *Targeted Residential Property Tax Rebate*
- (5.) *Temporary User Fee Reductions*

The analysis revealed that the countercyclical fiscal policy tools available to The City of Calgary are limited, as is The City's fiscal capacity to utilize those tools. In addition, many local stimulus policies may be less effective than broader initiatives from the federal and provincial governments. Thus, The City can only play a limited and secondary role in providing economic stimulus.

The constraints and opportunities

The significant constraints The City faces in deploying these tools are the limited ability to run deficits and the one-to-one correspondence between property taxes and government operating expenditures. It means that reducing taxes to provide relief would decrease spending by default.

Addressing this constraint would require saving up funds in reserves to prepare for unexpected future downturns. It creates an opportunity to review the extent to which existing reserves have that built-in capacity. Once a downturn has passed, reserves should be replenished promptly to prepare for the next time stimulus is needed.

The costs and benefits of using the tools

The costs of economic stimulus during a downturn must be paid for during times of economic strength. Spending increases or tax cuts during a downturn must be offset by spending decreases or tax increases during good years.

In a high inflation environment like the current one, saving for future spending could be less efficient than deficit-financing, as tax dollars collected today will have reduced purchasing power

Establishing Policy to Respond to Economic Highs and Lows

in the future. To ensure that the benefits outweigh the costs, The City would have to earn a rate of return on the savings that will recover the cost of purchasing power increases.

Best practices for applying policy tools

The analysis revealed five best practices for applying these policy tools:

- (a.) *Speed of Response*: The City has taken countercyclical actions in response to past economic downturns, despite its limitations as a municipal government. For example, The City implemented various relief programs following the oil price crash of 2015-2016 and during the COVID-19 pandemic. However, historical policy responses by The City have often occurred with a delay, with the full effects not being seen until as much as a year after the onset of a downturn. Attachment 2 offers detailed suggestions for responding more quickly in the future.
- (b.) *Public Communication*: Calgarians can benefit from understanding how different countercyclical fiscal policies work, why the federal and provincial governments have better capacity and effectiveness in enacting such policies, and how The City can play a secondary role in filling the gaps in federal and provincial programs within its current fiscal capacity.
- (c.) *Effective Targeting*: The negative impacts of an economic downturn are usually felt most strongly by vulnerable groups of people and small businesses in Calgary. Municipal relief programs targeting those groups provide greater economic stability in the long run and make Calgary a more desirable place to live and work.
- (d.) *Strong Partnerships*: Different funding sources could support countercyclical stimulus initiatives. While the federal and provincial governments frequently rely on deficit financing for their countercyclical policies, The City faces strict limitations on deficit financing for operational spending. The City of Calgary can request increased transfers from the provincial and federal governments; success would require clear messaging and robust intergovernmental partnership.
- (e.) *Fiscal Limits*: Evidence supports The City of Calgary not pursuing countercyclical fiscal policy actions beyond its current capacity.

The next steps for City Administration are:

- *Policy Development*. Developing a formal countercyclical fiscal policy for Council approval. The policy would guide Administration in developing responses and actions to moderate the impact of economic fluctuations. High inflation and central bank actions globally have increased the risk of a future recession making formal policy development a priority.
- *Appropriate Triggers*: Beyond the preference order for applying the identified tools, the appropriate tools to use at a given time must be decided in the context of the existing challenges. Appropriate triggers would need to be outlined to govern the use of these tools. The policy would need to outline these triggers.
- *Built-in Capacity Assessment*: The City's only option for independently funding countercyclical policy is using reserves. Rather than creating a new reserve for countercyclical fiscal policy, it is preferable to adapt the purpose of existing reserves like the Fiscal Stability Reserve. It creates an opportunity to review the built-in capacity of existing reserves for that purpose.

STAKEHOLDER ENGAGEMENT AND COMMUNICATION (EXTERNAL)

- Public Engagement was undertaken
- Public Communication or Engagement was not required
- Public/Stakeholders were informed

Establishing Policy to Respond to Economic Highs and Lows

Stakeholder dialogue/relations were undertaken

Although the work of the Financial Task Force included a targeted engagement process with key external partners, there was no public communication or engagement for this specific implementation-related report.

The Financial Task Force Implementation Steering Committee included external experts. These interested parties provided input into the development of this report.

IMPLICATIONS

Social

Many potential tools for economic stimulus provide direct benefits to specific segments of the city's population. Given the effects of different countercyclical policy tools on equity, those policies that reduce rather than exacerbate income inequality during a downturn are preferred, which aligns with the equity consideration of The City's Social Wellbeing Policy.

Environmental

Shifting the time profile of investments can support both fiscal and environmental sustainability. Investments needed to lower carbon emissions can be made earlier as part of the approach to executing countercyclical actions during a downturn. It is another rationale for the order of preference for the policy tools. Incorporating these considerations into stimulus packages can stabilize the economy, reduce investment needs during future austerity and help achieve climate targets.

Economic

The content of this report aligns with The City's Business Friendly Initiatives and Economic Resilience Strategy. The Business Environment pillar of Calgary's Economic Strategy is also advanced.

Using countercyclical policy to support the local economy during economic downturns could help prevent some of the closures of local small businesses. Temporary stimulus programs could also reduce unemployment and support the efficient utilization of Calgary's workforce. Increased economic stability over the long term could also encourage investment in Calgary.

Service and Financial Implications

No anticipated financial impact

The recommendations in this report have no direct financial impacts. Looking ahead, The City currently has reserves that could be used for future countercyclical fiscal policy. However, enhancing The City's capacity to implement countercyclical fiscal policy may require additional investment or changes to the optimal uncommitted balance of reserves.

Establishing Policy to Respond to Economic Highs and Lows

RISK

Intergovernmental risks exist if The City begins to advocate its role beyond its current role within provincial legislation and starts to provide countercyclical fiscal policy. If an expectation is created that The City will enact its countercyclical fiscal policy beyond current capacity, the provincial government may withhold additional transfers for The City during a downturn or forego local stimulus projects in Calgary. The provincial government may use this opportunity to reduce its efforts. Clear messaging regarding why The City is pursuing countercyclical fiscal policy may assist to mitigate issues. Likewise, cultivating strong partnerships with other orders of government may also reduce risks.

There may be financial sustainability risks since the timing and severity of future downturns are unknown, and reserves' optimal size and replenishment timeline is uncertain. If a future downturn is long-lasting, reserves may be insufficient to maintain the stimulus needed. However, if a future downturn is shorter and milder than expected, over-saving in reserves in the current high inflation environment may be more costly than in a low inflation time due to the loss of purchasing power over time.

Risks of unintended consequences exist as the actual economic stimulus effect of a specific fiscal policy action is uncertain. In addition, price inflation may result from economic stimulus if a sector cannot increase production in response to the stimulus.

ATTACHMENT(S)

1. Background and Previous Council Direction
2. Countercyclical Fiscal Policy Options for Calgary
3. Presentation

Department Circulation

General Manager	Department	Approve/Consult/Inform
Carla Male	Corporate Planning and Financial Services	Approve
Chris Arthurs	People, Innovation and Collaboration Services	Inform
Doug Morgan	Operational Services	Inform