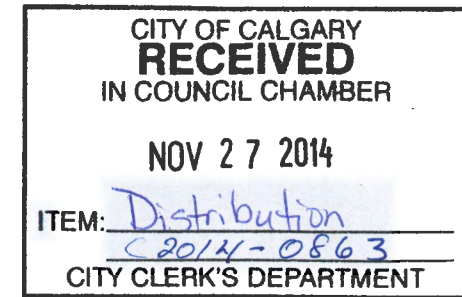


## 2014-15 Second Quarter Provincial Fiscal Update Analysis

November 26, 2014



In the latest budget update the Government of Alberta announced that it achieved a \$3.3 billion operational surplus in the first six months of fiscal year (FY) 2014-15. This amounts to an improvement of nearly \$1.8 billion from the projections laid out in *Budget 2014*. The amelioration was entirely attributable to operational revenues, which have so far surpassed original expectations by \$1.9 billion. Operational expenses were \$147 million higher than anticipated. Overall for FY 2014-15, the operational surplus is expected to come in at \$2.7 billion in spite of plunging oil prices. While this constitutes a \$62 million increase from the *Budget 2014* forecast, the estimate was slashed by nearly half a billion dollars from the first quarter budget update. The slight improvement from the original budget document stemmed from higher operational revenues outweighing rising operational expenditure expectations.

Operational revenues in the first half of FY 2014-15 were pegged at \$23.7 billion, which is \$1.9 billion higher than originally anticipated. The majority of the improvement was due to non-renewable resource revenues, which overshot *Budget 2014* projections by \$1.5 billion.

Provincial coffers will not benefit nearly as much from resource revenues in the second half of FY 2014-15. Overall for the current fiscal year, resource revenues are now expected to amount to \$9.4 billion. While this marks an improvement of \$146 million from the original forecast, it implies that revenues from non-renewable resources in the second half of the year will dive by roughly 50 per cent from the first six months of FY 2014-15. The Government of Alberta has slashed its forecast for average WTI oil prices to US\$88.88/barrel, down from US\$95.22/barrel in *Budget 2014* and US\$96.69/barrel in the first quarter fiscal update. However, there was also some good news. The forecast for the light-heavy crude oil differential has dropped considerably. The expected gap between WTI and WCS oil prices has narrowed from US\$25.00/barrel in *Budget 2014* to US\$18.16/barrel. Natural gas prices will lend further support to revenues, as the Alberta Reference Price is expected to average C\$4.01/GJ this year, up from original expectations of C\$3.29/GJ. Moreover, the provincial government now anticipates a slightly weaker Canadian dollar. This will offset some of the negative effects of lower oil prices, which are priced in U.S. dollars. Economic growth in 2014 is expected to remain robust, and income taxes will also lend increasing support to operational revenues. Personal income taxes are now anticipated to come in \$118 million higher, while corporate income taxes will exceed original projections by \$206 million. Investment income will add another \$86 million in upside. Overall, total operational revenues for FY 2014-15 are expected to be \$593 higher than the estimates presented in *Budget 2014*.

Meanwhile, on the other side of the ledger, operational expenses for the first half of the fiscal year came in \$147 million higher than anticipated. Disaster assistance expenditures, excluding those for 2013 flood assistance, exceeded original estimates by \$204 million due to overages in forest fire-fighting and agriculture indemnities. This overage was counterbalanced somewhat by lower operating and endowment fund

expenses. For the entirety of FY 2014-15, operational expenses are expected to hit \$41.0 billion, exceeding *Budget 2014* estimates by \$531 million as operating expenses pick up.

The Alberta economy has managed to outperform *Budget 2014* expectations so far, but 2015 forecasts for real GDP and employment growth were both lowered 0.2 percentage point to 2.8 per cent and 2.0 per cent, respectively. The provincial government's expectations for 2015 corporate profits, also known as net corporate operating surplus, have gone from a 4.0 per cent increase in *Budget 2014* to a contraction of 17.1 per cent.

The latest budget update is fairly cautious in its expectations for future revenues and economic growth, but the current energy price environment leaves plenty of room for both upside and downside risk. Until oil prices stabilize, evaluating Alberta's short-term fiscal prospects will be extremely challenging.

Major Changes of Key Financial Indicators: (Millions of \$)						
	First six months of FY 2014-15, ended September 30			FY 2014-15		
	Budget 2014-15	Actual	Change	Budget 2014-15	Q2 Fiscal Update	Change
Operational Revenue	21,831	23,728	1,897	43,076	43,669	593
Personal Income Taxes	5,497	5,540	43	11,153	11,271	118
Investment Income	1,235	1,507	272	2,472	2,558	86
Non-Renewable Resource Revenue	4,686	6,201	1,515	9,209	9,355	146
Transfers from Govt of Canada	3,122	2,942	(180)	6,234	6,154	(80)
Operational Expense	20,260	20,407	147	40,432	40,963	531
Operational Surplus/(Deficit)	1,571	3,321	1,750	2,644	2,706	62

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