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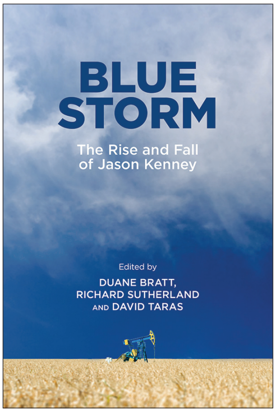

BLUE STORM: THE RISE AND FALL OF JASON KENNEY

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The Long Slide towards Fiscal Reckoning: Managing Alberta's Finances in an Age of Decline

Trevor Tombe

Introduction

In an early April 2020 televised address, Alberta's Premier Jason Kenney delivered grim news about the COVID-19 pandemic. It was not only a health crisis, but an economic and fiscal one as well. "[Albertans] will face a great fiscal reckoning in the future," he warned.[1] But while the significant disruptions from the pandemic accelerated many of the fiscal pressures facing Alberta, it was by no means the cause. In a very real but underappreciated sense, Alberta has been managing a steady fiscal decline for over four decades. Successive governments have responded to this in different ways, though none—including the new United Conservative Party (UCP) government—have fully come to grips with the scale of the challenge. Despite recent increases in global oil and gas prices—leading to historically high levels of resource revenues for the province in 2022—Alberta's long slide towards fiscal reckoning continues. And fiscal, economic, and political constraints to substantive reforms mounted during the UCP's term and will continue to pressure future Alberta governments.

Managing public finances is never easy, of course, though it is especially difficult in Alberta. Large and unexpected swings in revenues create short-term challenges that would be difficult in the best of times.

But steadily and consistently declining revenues in recent decades creates increasingly binding constraints on the government's range of action. Alberta's heavy reliance on revenues from natural resources—primarily natural gas and oil sales—is behind both its recent short-term challenges and its future long-term ones. And while not a new development, managing Alberta's dependence on resource revenues is more difficult for the current government than past ones. Significant economic disruptions, a rapidly aging population, a shrinking gap between Alberta and other provinces, and a political atmosphere averse to thoughtful compromise all make fiscal policy more difficult. Despite this, Alberta's still notable economic strength, and the potential for strong future growth, provides options. In this chapter, I explore the nature of Alberta's fiscal decline, analyse its prospects going forward, and identify how the new UCP government has managed provincial finances. In short, the challenges are significant, but there are several options to address them. An important legacy of the UCP first few years in office, however, may be in having made these challenges more difficult to overcome.

Before unpacking the fiscal challenges that Alberta faces, a broad overview of its budget and recent political developments is necessary. As with other Canadian provinces, the bulk of program expenditures are accounted for by a few core functions: health care, education, and social services. Combined, these activities account for approximately three-quarters of total program expenditures in the province—which is a similar pattern observed elsewhere. Other areas, such as agriculture, environment, infrastructure, justice, transportation, and so on, are all critical but relatively insubstantial for the overall budget. This high degree of expenditure concentration is important to appreciate because any move to restrain spending growth or reduce spending outright will unavoidably affect health care and educational services. It also means changes in demand for these services—primarily through demographic changes—will have large implications for Alberta's fiscal future.

On the revenue side, Alberta differs in several important ways from other provinces. First, taxation funds a uniquely small share of public services. In the 2019/20 fiscal year, before the pandemic hit, tax revenues were just over $19 billion—equivalent to approximately one-third of total government spending. By contrast, Canadian provincial governments, on the whole, fund slightly more than half of total spending using tax revenues. Alberta's lower taxation revenues, due in part—though not exclusively—to its lack of a general sales tax, are (typically) made up for by far larger than average amounts of investment income and natural resource revenues. The former is from over $21 billion in savings within the Alberta Heritage Fund plus related endowments. The latter is primarily from royalties on oil and gas production, especially bitumen in recent years. This dependence is the central fiscal policy challenge for Alberta both in the short-term and the long. Overall, as I will show, roughly one-quarter of total revenues to the Alberta government needs to come from natural resource revenues to balance the budget.

Unfortunately for the government, disappointing oil prices since 2014, however, have made that impossible. It is also the proximate cause of recent political turmoil and of the UCP's eventual rise. From an average of nearly $100 per barrel (USD WTI) between 2011 and mid-2014, oil prices fell to less than $50 per barrel by January 2015 and to $30 per barrel by early 2016. Although many prior governments ran modest budget deficits, this decline in price dramatically increased provincial borrowing. "We are at a turning point in our province," said former Alberta Premier Jim Prentice in a televised address on March 24, 2015. "We need to get our program expenditures off the energy revenue rollercoaster and make our revenues more secure," he continued.[2] Alberta's budget that year (tabled, though never passed) detailed a comprehensive plan to ease reliance on resource revenues through a combination of real per capita expenditure reductions, meaningful tax increases, and gradually saving an increasingly large portion of natural resource revenues. But this plan was not to be. The Prentice government was defeated in an historic election in 2015 that brought the New Democratic Party (NDP), led by Rachel Notley, to power.

Instead of continuing the reform of Alberta's fiscal policy, the new government quickly opted to shelve Prentice's plan and continue the same general fiscal and economic strategy of previous Progressive Conservative (PC) governments in the years prior to the 2014 oil price decline. That is, they opted growth spending in line with population and prices while making only modest changes in tax rates and structures. Their hope was the same as past PC governments: rebounding oil prices and production would spare the government from making difficult budget decisions.

These hopes had regularly been dashed in the past, but it remained a central pillar of the NDP's longer-term fiscal plans. Their "Path to Balance" in early 2019, for example, which was released shortly before the election campaign that year, was based almost entirely on rising oil prices and resource revenues. It required nearly $12 billion in natural resource revenues to balance by 2024.[3] But this too was not to be and the NDP were defeated at the polls—at least partially due to public concerns over rising deficits.

Following their election in April 2019, the UCP under Jason Kenney introduced their first comprehensive fiscal plan in late October that year. Unlike previous governments who largely held the line, their plan centred on shrinking the size of government. In the year prior to their election, total operating expenses of the Government of Alberta exceeded $48.4 billion, but by 2022/23 the UCP planned to reduce this to $47.1 billion.[4] While a modest aggregate reduction of only 2.7 per cent, the real level of spending per person is substantially lower. The budget projected population growth of 7.5 per cent by 2023, for example, and overall price inflation of nearly 8 per cent over that same time. For operating expenses to merely keep pace with population and inflation, an increase of over 16 per cent would therefore be required. And relative to the NDP fiscal plan for 2022/23, I estimate operating expenses were actually lowered by $7 billion or nearly 13 per cent that year. This is large. Excluding health, education, and child and social services, total government operating expenditures in all other areas of government, for comparison, was less than $9.3 billion in 2018/19.

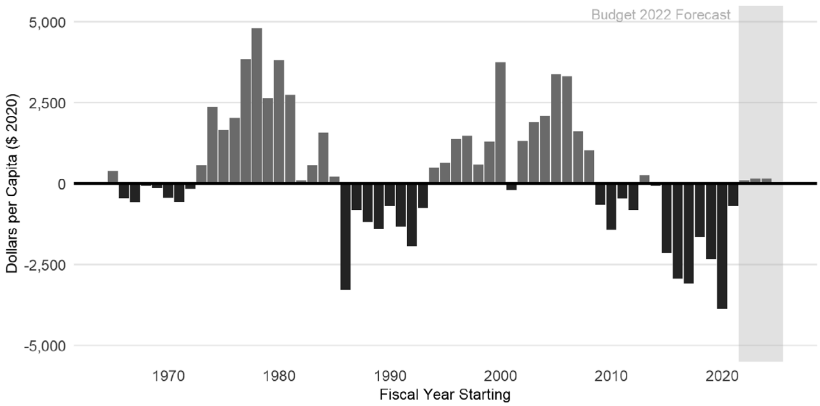
On the revenue side of the UCP fiscal plan, while there were modest increases in some areas, the government's overall plan was to reduce or eliminate taxes. It lowered the corporate tax rate from 12 per cent to 8 per cent (phased gradually over time) and eliminated one of Alberta's two carbon taxes (the one on retail fuel that individuals see) (see Duane Bratt's chapter). Along with other developments, the UCP plan projected total revenue by 2022/23 at $57.5 billion, or approximately $6 billion (9.4 per cent) less than the NDP fiscal plan for that year. Taken together, the UCP fiscal policy represents a meaningful reduction in the size and scope of the provincial government and was therefore a clear departure from previous governments. Looking beyond 2022/23, however, current fiscal policy falls short of addressing the gap between government revenues and expenditures and, more importantly, is ill-prepared to address longer-term challenges. These challenges pre-date COVID, but the economic and fiscal disruptions from the pandemic added significantly to them.

The Effect of COVID-19 on Alberta Finances

The pandemic took a fiscal toll on all provincial governments, though costs to Alberta were particularly large (see also Lisa Young's chapter). Economic disruptions from the pandemic, including significant employment losses and business closures, meant provincial revenues from a variety of sources fell sharply. In addition, rising direct program expenditure within health care and for individual and business income supports added to the deficit. The original fiscal plan in Budget 2019 targeted a deficit of $5.9 billion for fiscal year 2020/21. The actual deficit for the year came in at $17 billion.[5] For additional context, I illustrate the past half century of Alberta surpluses and deficits in Figure 12.1, adjusted for inflation and population growth over time. Though the borrowing through the pandemic was high, so too were the years leading up to, for reasons discussed earlier. But at approximately $3,800 per Albertan, I estimate the 2020/21 deficit—though smaller than some feared early in the pandemic—was the largest in Alberta's history.

The full fiscal implications of the pandemic are not yet known, but recent Government of Alberta budgets provide a good first look.[6] Total income tax revenues, from individuals and corporations, were $2.9 billion lower in 2020/21 than was previously projected in Budget 2019 for that same fiscal year. Other tax revenues sources also declined significantly, notably gasoline taxes as fuel purchases during the early months of the pandemic were very low, and revenues from gaming and lottery activities fell in half, from a planned $1.4 billion to $774 million. Finally, as this chapter will explore in greater detail later, Alberta's reliance on revenues from natural resources also posed a challenge. Global oil prices declined precipitously during the pandemic, and therefore natural resource revenues to Alberta fell as well—by nearly $2.3 billion. Overall, excluding federal transfers, total revenues fell by nearly $8.6 billion due to pandemic-related disruptions. Cushioning this decline, however, were sharp increases in federal transfers. Total transfers to provincial and territorial governments in Canada rose in 2020 to its highest level since 1867, as a

Figure 12.1. Alberta Government Budget Balances, 1965/66 to 2024/25 (F)



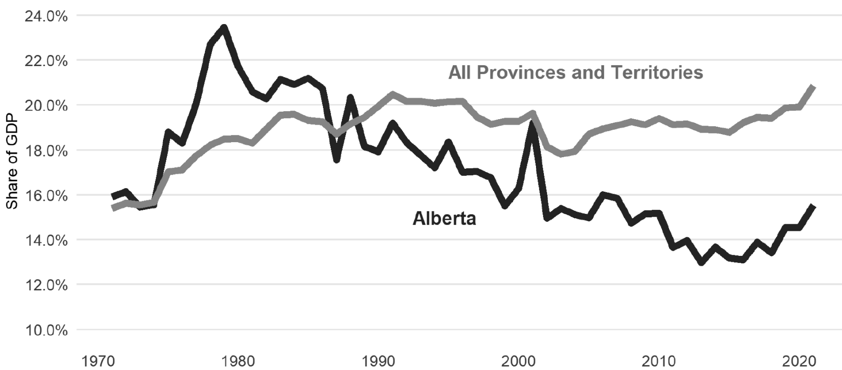
Sources: Own calculations from Finances of the Nation "Government Revenue and Expenditure" dataset, accessed 4 May 2022, and projections for 2022/23 onwards from Alberta's Budget 2022 (Government of Alberta, Fiscal Plan: Moving Forward (Alberta Treasury Board and Finance: Edmonton, 2022). Available at https://open.alberta.ca/publications/budget-2022).

share of the overall economy.[7] For Alberta, this meant a boost of roughly $1.4 billion in 2020/21.

Pandemic-related expenditures were also significant. In 2020/21, total operating expenditures related to COVID-19 and certain economic recovery initiatives approached $4.1 billion. Much of this was increases in health expenditures, which reached nearly $1.1 billion (see Gillian Steward's chapter). Other significant costs included support to municipal governments ($621 million), to schools ($248 million), to children and social services ($229 million), and more. Higher expenditures continued through to 2021/22 but are currently forecast to decline to $2.8 billion, and further to less than $500 million by 2023/24.

Disruptions to Alberta's broader economy compound these fiscal challenges. But as is evident in Figure 12.1, the shock of COVID-19 occurred following years of prior challenges. Indeed, it is difficult to overstate the scale of the shock that started in 2014. Between 2014 and 2016, I estimate the province's nominal GDP per capita fell by roughly one-fifth—larger

Figure 12.2. Government Revenues as a Share of GDP, 1970/71 to 2020/21



Note: The increase in 2020/21 total revenues as a share of GDP is largely due to contracting economic activity that year due to the COVID-19 pandemic.

Sources: Own calculations from Finances of the Nation "Government Revenue and Expenditure" dataset. Accessed 4 May 2022.

than the contraction due to COVID-19—and roughly corresponds to how much lower total incomes are in the province. The recovery from this decline was also slower than many hoped for, and sharply interrupted by the pandemic. Only by 2024 does the government project that Alberta's overall economy will return to pre-pandemic levels. This is an historically significant period of economic decline. Using long-run provincial economic data, I find only three other periods compare.[8] First, following the First World War, Alberta's per capita level of economic activity contracted by approximately 30 per cent and remained relatively flat for many years through the droughts and agricultural challenges of the 1920s. Second, the Great Depression hit all regions hard, to be sure, but it hit Alberta and other agriculturally oriented regions hardest. By 1933, I estimate Alberta's real GDP per economy was roughly half what it was in 1929. And it only gradually recovered from there. Finally, the 1986 oil price drop was the most recent comparable period with Alberta's economy contracting by roughly one-fifth per capita and remaining there for nearly a decade until growth resumed in the late 1990s. But unlike this most recent comparable contraction, Alberta faces a confluence of mounting fiscal pressures and far less room to maneuver, despite recent increases in resource revenues helping balance the provincial books in 2022.

Alberta's Long Fiscal Decline

Declining natural resource revenues has been the central short-term challenge facing several successive Alberta governments. Recent increases due to rising global oil and gas prices, especially following the Russian invasion of Ukraine, are helpful to ease these challenges but this is a temporary reprieve from longer-term challenges.

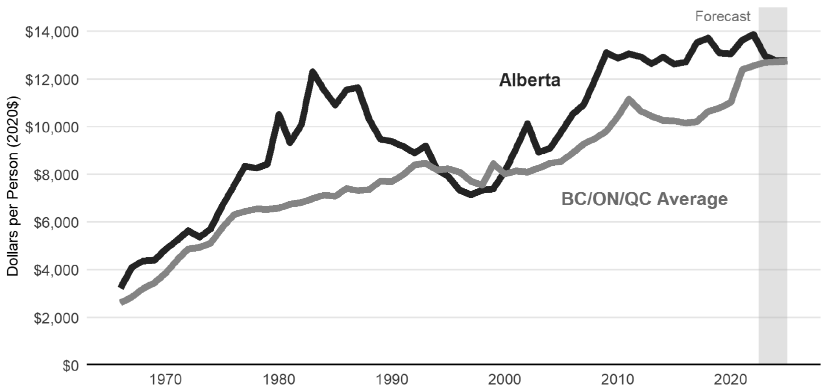
The scale of Alberta's long fiscal decline is not broadly appreciated and one Alberta has not yet come to grips with. Over the past forty years, total government revenues as a share of the province's overall economy declined by nearly ten percentage points. And this is entirely accounted for by falling natural resource revenues, as displayed in Figure 12.2. In 1979, when government revenues were highest at roughly 24 per cent of GDP, natural resource revenues alone were 12 per cent—or half of the province's total. By 2019, total government revenues declined to 14.5 per cent of GDP and natural resource revenues to less than two. More precisely, total revenues declined roughly ten percentage points over this period and natural resource revenues declined slightly more. Meanwhile, other provincial and territorial governments in Canada gradually increased their revenues from approximately 15 per cent to 20 per cent between 1970 and 1990, remaining relatively stable thereafter. Alberta's experience is markedly different and the entire story of the province's fiscal challenge over these decades is one of declining revenues from oil and gas. This is the fundamental fiscal challenge facing Alberta, and one that appears increasingly difficult for successive governments to confront. Recent increases in natural resource revenues in 2021, which may potentially increase in subsequent years, does not fundamentally change this picture. In 2021/22, for example, Budget 2022 projects natural resource revenues in excess of $13 billion—but this is less than 3.7 per cent of GDP. Higher than recent years, but a small increase relative to the province's long-run decline.

Historically, Alberta governments responded to this long slide in different ways. At first, there was considerable space in Alberta's budget to absorb the revenue decline through shrinking surpluses, gradually declining shares of natural resource revenues that were saved in the Alberta Heritage Savings Trust Fund and using income from that fund towards government operations. In 1982/83, for example, a portion of income from the fund was shifted into general government revenue.[9] And one year later, the share of resource revenues saved was cut in half. During moments of sharp and unexpected declines in revenue, however, more dramatic changes were required.

Consider the large decline in natural resource revenues in 1986, when resource revenue declined from over $4.9 billion to $1.9 billion. In response, Budget 1987 featured a mix of tax increases and expenditure cuts to achieve what they hoped would be a balanced budget by 1990/91. The strategy was "a three-pronged attack on the deficit," said Finance Minister Johnston during the budget address, but one whose actions "will be fair and those Albertans in need will be protected."[10] First, the government undertook a detailed review of expenditures to reduce spending but in a manner to "have the least possible adverse effect on Albertans." Health, education, and social services were largely spared but other program expenditure areas declined by an overall average of 25 per cent by 1988/89 compared to 1985/86. Second, contributions to the Heritage Fund were ended, which boosted resource revenues available for the general budget. Finally, there were tax increases—substantial ones. The government increased the province's basic income tax by 7 per cent,[11] introduced an 8 per cent surtax on high-income individuals, levied a new one percentage point flat tax on all incomes, increased tobacco taxes by one dollar per pack, increased liquor markups, introduced a 5 per cent tax on hotel rooms, increased gasoline taxes by 5 cents per litre, increased the corporate income tax from 10 to 15 per cent, and more. These were large increases. Relative to total taxation revenues, I estimate these increases are equivalent to approximately $7 billion per year today.

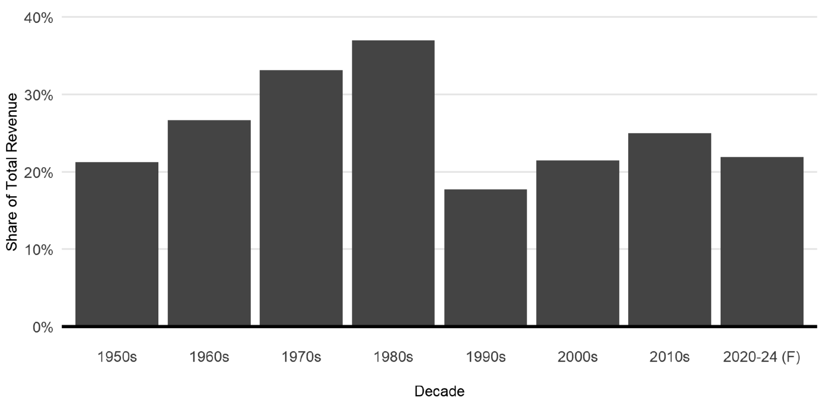
This mixed approach of both expenditure reductions and revenue increases were deliberately chosen by Premier Getty's government. They had the luxury of large revenue and expenditure side options to fill the hole left by falling resource revenues. The subsequent government under Premier Klein, however, had different priorities and when additional fiscal actions were necessary following the recession of the early 1990s, the government

Figure 12.3. Real Per Capita Provincial Program Spending, 1965/66 to 2024/25 (F)



Sources: Own calculations from Finances of the Nation "Government Revenue and Expenditure" dataset, accessed 4 May 2022, and projections for 2022/23 onwards from various provincial government budgets.

Figure 12.4. Resource Revenues Required to Balance Alberta's Budget (As a Share of Total Revenue)



Sources: Own calculations from Boothe, Kneebone and Wilkins, and the Government of Alberta's Budget 2022. Recent years are presented on a fiscal plan basis. (Paul Boothe, *The Growth of Government Spending in Alberta* [Canadian Tax Foundation: Toronto, 1995]; Ronald Kneebone and Margarita Wilkins, "Canadian Provincial Government Budget Data, 1980/81 to 2013/14," Canadian Public Policy [2016] 42 [1], 1–19. Updated February 2021.)

more aggressively pursued program-spending reductions. Specifically, the government lowered program-expenditures by roughly the equivalent of $3,000 per person today. I illustrate this in Figure 12.3. Combined with significant and rising natural resource revenues later in Premier Klein's mandate, the government was able to avoid deep reforms to the province's fiscal policy to eliminate its dependence on natural resource revenues. Today, a similar focus on expenditure restraint is sufficient to overcome Alberta's short-term fiscal challenges only due to rising natural resource revenues from high global oil prices. In future years, absent continued increases in resource revenues, spending restraint alone may prove insufficient. And with Alberta nearly aligned with other large provinces in Canada, the scope for such restraint may also be less than it has been historically.

Challenges Facing the UCP's Fiscal Policy

Despite recent increases in resource revenues, Alberta's long slide towards a fiscal reckoning may soon be unavoidable. Managing this will be more difficult for governments today than it has been in the past. The scale of the provincial government's dependence on resource revenues remains high, the scope for program-expenditure reductions is limited, economic disruptions make raising revenue more difficult, and long-term spending pressures from an aging population and a coming bulge in the number of post-secondary-age students must be accommodated. I unpack in detail each of these and explore how they may challenge the UCP's approach to fiscal policy.

First, the provincial government's dependence on natural resource revenues is as high as ever. Since the 1990s, when our reliance on resource revenues was lowest—due to large spending reductions by the former PC government under Premier Klein just discussed—our reliance has steadily increased. Since 2010, for example, the government has required one-quarter of all revenues to come from natural resources to balance its books. Though not near its historic highs, this is significant. I display this measure in Figure 12.4, projected forward using the latest fiscal forecasts from Budget 2022. The short-term risks that come with funding public services with a volatile revenue source will therefore remain. More challenging, though, are the long-term risks of falling oil and gas revenues as the global energy transition accelerates. Serious efforts to get off the "energy revenue rollercoaster," as Premier Prentice put it, were abandoned by the former NDP government and current UCP government alike. They instead largely hoped for rebounding oil prices and production to spur not only economic recovery but also patch the government's fiscal holes. Since 2021, this strategy has paid off for the government, but historically high resource revenues may provide only temporary relief as longer-term pressures mount.

Reducing Alberta's dependence requires lower spending growth, higher revenues, or some combination of the two. Relying on only one side of the budget or the other requires infeasibly large changes. For perspective, by 2023, a general sales tax harmonized with the GST would need to be approximately fourteen percentage points—far beyond rates found elsewhere in Canada. Alternatively, existing tax rates would need to rise by two-thirds across the board. On the expenditure side, the entire combined budgets of the Ministries of Education and Advanced Education would need to be eliminated. And if health, education, and social services were protected, cutting every single dollar of spending in all other areas of government operations would fall short of what's needed. In short, gradual moves on both the revenue and the spending side of the budget would be required to address Alberta's fiscal challenges. Something on the order of achieving spending parity with other large provinces, growing with population and inflation thereafter, and phasing in a broad sales tax of approximately 5 per cent could eliminate Alberta's reliance on resource revenues fully sometime in the 2030s.

High resource revenues are, of course, a boon that governments have difficulty resisting when they happen—as they are now. Following Alberta's Budget 2022, released in late February 2022, for example, the originally projected deficit for 2021/22 fell from $18.2 billion projected in Budget 2021 to just $3.2 billion in Budget 2022.[12] A massive decline largely accounted for by natural resource revenues rising to over $13 billion for the year. Future fiscal years have also improved, with modest surpluses projected in Budget 2022 for 2022/23 onwards. High resource revenues, however, merely paper over the underlying fiscal risk that the provincial budget is exposed to. And over the longer run, global climate polities and the gradually accelerating energy transition will eventually—and permanently—eliminate these revenues as a meaningful contributor to Alberta finances. But by saving resource revenues today, a physical asset whose value may not last can be transformed into a financial one that can be maintained in perpetuity. To date, however, successive governments have resisted even contemplating any policy like what former Premier Prentice put forward in 2015.

The second challenge facing the UCP directly constrains their preferred policy option. In stark contrast to previous Alberta governments, the scope for expenditure reductions is significantly narrower today. As illustrated in Figure 12.3, the government's previous ability to engage in this significant spending reduction was substantial. The gap between Alberta average spending and other major provinces, for example, was over $6,000 per person in the early 1980s. The expenditure reductions during Premier Getty and Klein's early years shrank this gap, though it increased again from 2000 onwards. Today, the gap between Alberta program spending and those same provinces is smaller. And the UCP's fiscal plan enacted in Budget 2019 and re-committed to in subsequent budgets will bring average spending in Alberta in line with other large provinces by 2022/23. Despite that, a large deficit would remain were it not for increases in resource revenues because taxation revenues are far below levels found elsewhere. Today, Alberta maintains the second lowest average rate of income taxation, the lowest rate of gasoline taxes, does not have a payroll tax, health care levies, nor—most importantly—does it levy a general sales tax. The only province with lower income taxes is British Columbia, but it can do so because of provincial carbon tax revenues, general sales taxes, and health care premiums. The ability of the UCP to enact greater expenditure reductions than currently planned may therefore be limited.

The composition of spending today is also more constraining than in the past. Past governments had greater scope for spending restraint outside of core areas of health care, education, and social services. In 1985, for example, only slightly more than half of total program spending was in those areas. Today, that share has increased to three-quarters—driven largely by increases within health care. Looking forward, expenditure pressures on provincial governments will be incredible. Significant public sector compensation restraint may be unavoidable. This isn't a new development. The previous NDP government, for example, pursued public sector compensation freezes in its negotiations. The UCP, in contrast, originally pushed for wage rollbacks on the order of 3–5 per cent. Importantly, a wage freeze is an effective real reduction in compensation as inflation erodes the purchasing power of each dollar earned. With inflation averaging around 2 per cent per year, the NDP and UCP approaches to public sector compensation are not materially different over a multiyear horizon. They differ primarily in the speed of implementing public sector compensation reductions, but also in their public communications on the issue.

The UCP consistently opts for combative and adversarial language, which is a marked departure from prior governments. In a fiscal update in November 2020, for example, the government wrote that the public sector "does not create jobs or generate wealth,"[13] despite the significant role played by many to improve lives and livelihoods during the pandemic. And, to highlight another example, the Alberta finance minister accused the United Nurses of Alberta of engaging in a "a shameful effort to take advantage of a health crisis" during negotiations.[14] This polarizing rhetoric may complicate future negotiations. To be sure, the additional fiscal room provided by boosted resource revenues allowed the government to agree to modest nominal wage increases for several public sector unions. This helped avoid significant labour disruptions in the year prior to the provincial election. Historically high inflation, however, which reached 6.7 per cent in March 2022, effectively makes a 1 per cent nominal increase equivalent in real terms to what a 3 per cent nominal rollback would have meant if inflation remained near at its normal level. If higher rates of inflation continue, negotiations could become especially challenging once again in the coming years.

These are but short-term considerations; the longer-term ones are even more daunting. Canada's population is growing older. By 2050, Statistics Canada's medium-case projection anticipates approximately one in four Canadians will be age sixty-five or older. This is significantly above the one in six today and double the one in eight who were above sixty-five in 2000. By 2050, there may be as many individuals over the age of 80, as a share of the population, as there were those over sixty-five in 2000. While Alberta is currently the youngest province by a wide margin, and will continue to be in these scenarios, it will not be spared the pressure on government budgets. This population aging will pressure public finances through rising health care costs and declining rates of economic growth.

The direct effects on health expenditures can be quantified in a straightforward way. The Canadian Institute for Health Information estimates that the average person aged sixty-five and over accounts for approximately $15,000 per year in provincial government health care spending and those over age eighty account for nearly twice that—at over $27,000 per year.[15] Younger individuals in their twenties and thirties, meanwhile, barely account for more than $3,000. As the share of the province's population among older age groups increases, health spending will almost surely rise. Combined with the typically faster pace of price increases for health care equipment and supplies than the overall rate of economy-wide inflation, rising health costs will be the most important source of increased government expenditure pressures for years to come. In previous research, I estimated that by 2050, rising health care spending will account for half of the total increase in government spending.[16] And overall spending on health will rise from just over one-third of total program expenditures in 2019 to nearly 45 per cent. For context, that increased share is equivalent to nearly $9 billion per year in additional health care expenditures today. Alberta is not yet ready for this, to say nothing of the full long-term implications of COVID-19 on the health system.

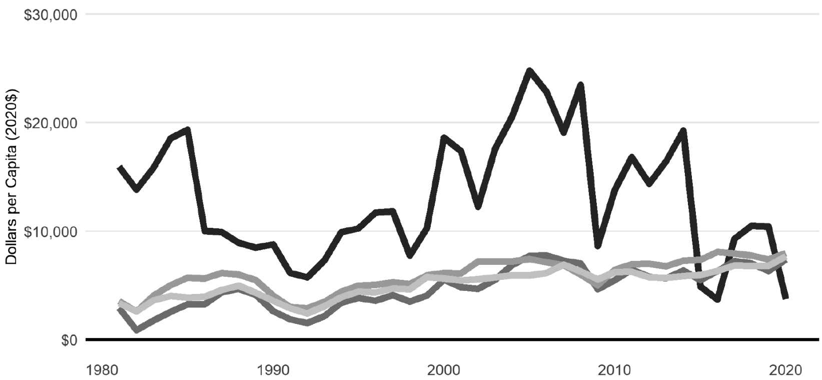
Budget pressures from an aging population go beyond health care expenditures. As more individuals retire and exit the labour force, total taxable incomes will naturally decline. If historic norms for labour force participation hold, I estimate Alberta's aging population implies approximately 0.3 percentage points slower economic growth over the next two decades. And since slower economic growth tends to lower household taxable incomes, government revenue growth will be correspondingly slow. Indeed, this revenue pressure may be greater in Alberta than elsewhere. Tax payments by elderly individuals, after all, tend to be accounted for mainly by property taxes and sales taxes.[17] Alberta has the former but lacks the latter.

Health care is not the only source of expenditure pressure facing Alberta soon. At the younger end of the age distribution, the population of individuals in typical post-secondary education age groups is set to rise significantly as well—starting as soon as 2024. Currently, there are approximately 380,000 Albertans between the ages of eighteen and twenty-four. The Government of Alberta projects this to remain relatively flat for the next couple years.[18] But between 2024 and 2034, the population growth of this age group may exceed the province's total growth rate by a half point per year—resulting in an increase of nearly 30 per cent by 2034 or over 100,000 persons. And in their high-growth scenario—one that presumably the government believes its economic recovery and growth policies would stimulate—this population increases by nearly 150,000. Not all will seek university or college admissions, to be sure, but fully 60 per cent of Albertans historically enroll in a post-secondary institution or registered apprenticeship program within six years of entering grade 10.[19] If this transition rate holds, there may be 60,000 to 90,000 more persons looking for space at already heavily constrained institutions in Alberta. Recent choices by the government to constrain university and college budgets will make it difficult to accommodate this growth, which may open the door to younger Albertans leaving the province to access space elsewhere.

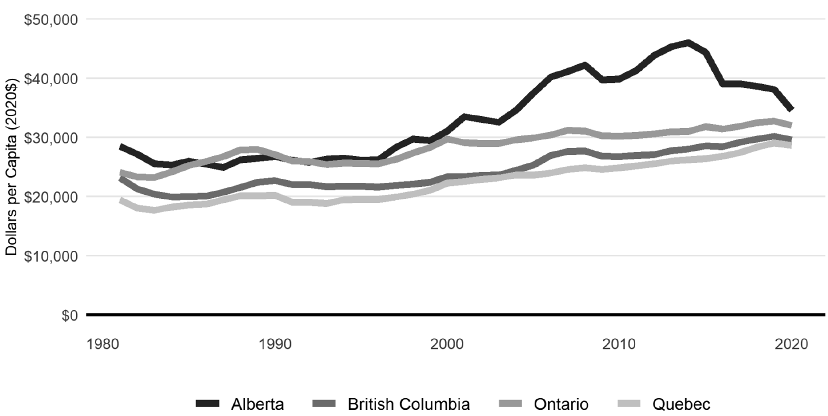
With such expenditure pressures mounting in several areas, tax increases will be increasingly difficult for governments to avoid. Luckily, a strong economy also allows Alberta's government to raise more revenues than identical tax rates would elsewhere. Economic pressures, however, make raising revenues more difficult than it was for past governments in Alberta. As discussed earlier in the chapter, Alberta's economy contracted significantly from late 2014 onwards as global oil prices collapsed. By January 2020, for example, average weekly earnings were no higher than five years earlier. Adjusting for inflation, they were over 10 per cent lower. Business incomes also declined significantly. And with lower incomes and corporate profits comes lower taxation revenues. Each point of corporate income tax, for example, raised over $500 million in 2014 but less than half that in 2021. Too appreciate the scale of this decline, I plot the per capita value of both corporate profits and total labour compensation in Figure 12.5. Both account for most income earned by Albertans, and—more importantly for government finances—are the largest tax bases in the province. As is evident in the figure, both have significantly declined since their peaks in 2014. Corporate profits, or more precisely corporate net operating surpluses, fell in half from nearly $20,000 per capita (in 2020 dollars) in 2014 to about $10,000 per capita five year later and to less than

Figure 12.1a. Real Corporate Profits and Labour Compensation per Capita

(a) Corporate Profits



(b) Labour Compensation



Note: Corporate profits here reflects net operating surpluses of corporate entities within the provincial economic accounts. This approximates, though differs from, accounting definitions of profit.

Sources: Authors' calculations from Statistics Canada data tables 36-10-0221-01, 17-10-0005-01, and 18-10-0005-01.

$4,000 in 2020. Total labour compensation has also declined in recent years, from $46,100 per capita in 2014 (in 2020 dollars) to $38,100 by 2019 and to less than $34,600 by 2020. Despite recent increases in oil prices—which has dramatically increased corporate profits—the general pattern that Alberta has converged to, which is something closer to normal levels of economic activity in Canada, may continue. If it does, this will dampen the government's ability to raises revenues through taxation.

Of course, two positives must not be neglected. First, though it has experienced a significant reduction, Alberta remains above where the other three large provinces in Canada are. Total labour compensation, for example, has declined by 25 per cent since 2014, but it remains approximately 8 per cent above Ontario levels and 20 per cent above Quebec's. This is also evident in Figure 12.5. Second, and more importantly, Alberta's large ups and downs appear firmly anchored by a nearly identical trend in rate of growth compared to other provinces. Long time-series data on provincial economic conditions are rare in Canada, but we do have nearly a century of data on household disposable incomes. This is the after-tax income that households have available to purchase goods and services or to save for the future. Between 2015 and 2019, average real disposable incomes fell 12 per cent. This is very large.

Indeed, that four-year decline is larger than at any point since 1929 through 1933. Despite such a large decline, Alberta remains a leader in Canada. And over the ninety-three years between 1926 and 2019, where Statistics Canada data on real household disposable income per can be compiled, the average growth over time in Alberta is like other regions, despite Alberta's far higher degree of volatility. On average, growth in real disposable incomes is 2 per cent nationally and 2 per cent in Alberta. If this historic average growth continues, then following Alberta transition to a level of income closer to the average—though still above most—it would take approximately six years to cover the drop experienced in the previous recession. Of course, COVID changes this picture, but does so for all. And given emergency response measures from the federal government, disposable incomes increased in 2020 and the post-COVID recovery has, so far, been robust. That complicating factor aside, by the sheer force of normal economic growth, Alberta households may see their living standards exceed their pre-recession peak by the latter half of the decade—continuing to improve thereafter. Sharp declines since 2014 do not imply the province's best days are behind it.

Conclusion

These fiscal hurdles are not insurmountable. Despite the large decline in Alberta's economy recently, it remains strong relative to other provinces. Average wages are higher than elsewhere, overall employment is a higher share of its population, and corporate profits remain robust. The need for fiscal adjustment stems from a ratcheting down in the overall level, though to one that remains enviable to other provinces. The UCP government did respond to recent fiscal shortfalls modestly but did so focused on the expenditure side of the budget and with moves that will likely prove insufficient. Worse, the combative political rhetoric of Premier Kenney specifically—and the UCP government generally—may constrain the government and complicate efforts to adapt provincial policies to Alberta's new fiscal and economic reality. Worse, the government's claims that much of Alberta's economic weakness is caused by hostile federal policies may also distract from necessary fiscal reforms that the province itself can adopt. Simply put, polarized political rhetoric may pay short-term dividends but at the cost of delaying action on, and therefore exacerbating, Alberta's long-term challenges.

Fiscal policy reforms will be increasingly necessary to ease Alberta off its resource revenue dependence and to accommodate pressures from an aging population. Several reasonable options are available thanks to Alberta's still enviable (though diminished) economic advantages, but none are easily adopted. Lower program spending and higher taxes impose real costs on Alberta's families and businesses. Public acceptance of difficult choices is necessary and requires clear, honest leadership. The fiscal realities facing Alberta make an all-of-budget approach unavoidable. By focusing heavily on the spending side of the budget, the UCP government delayed a broader and longer-term conversation about how Alberta recovers from the pandemic in a sustainable way.

Alberta is and has been on a long slide towards a fiscal reckoning. The only questions that now remains is how disruptive and divisive that reckoning will be.

NOTES

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3 Government of Alberta, *2018–19 Third Quarter Fiscal Update and Economic Statement* (Alberta Treasury Board and Finance: Edmonton, 2019), 36.

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6 *Ibid*.

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