

FISCAL POLICY TRENDS

September 2018

THE LONG-TERM CONSEQUENCES OF FISCAL RESPONSES TO RESOURCE REVENUE FLUCTUATIONS

By Ergete Ferede

Over the last half-century, the Alberta government has been heavily reliant on non-renewable resource revenues, which have averaged about 30 per cent of the provincial government's total revenue. This reliance poses a fiscal challenge as resource revenues are volatile and uncertain due to the vagaries of global energy price shocks, pipeline disruptions and other events such as the federal government's National Energy Program. This commentary shows that the Alberta government's budgetary responses to fluctuations in resource revenues have had long-term deleterious consequences for the province's fiscal health.

Our analysis of Alberta's fiscal responses to fluctuations in resource revenue from 1970-1971 to 2016-2017 indicates that a \$1 increase in real per capita non-renewable resource revenue is associated with a 56-cent increase in program spending in the following fiscal year. However, a \$1 reduction in resource revenue has not been followed by a reduction in program spending or a significant adjustment in other fiscal variables such as personal or corporate tax revenues.

These asymmetric budgetary responses to resource revenue shocks – increases in spending during booms and the absence of spending cuts or tax revenue increases during downturns – means that public debt ratchets up over time as downturns in resource revenue are not offset by saving resource revenue increases during booms.

Figure 1: Cumulative Change in Real Per Capita Net Financial Assets in 1000s 2017 \$

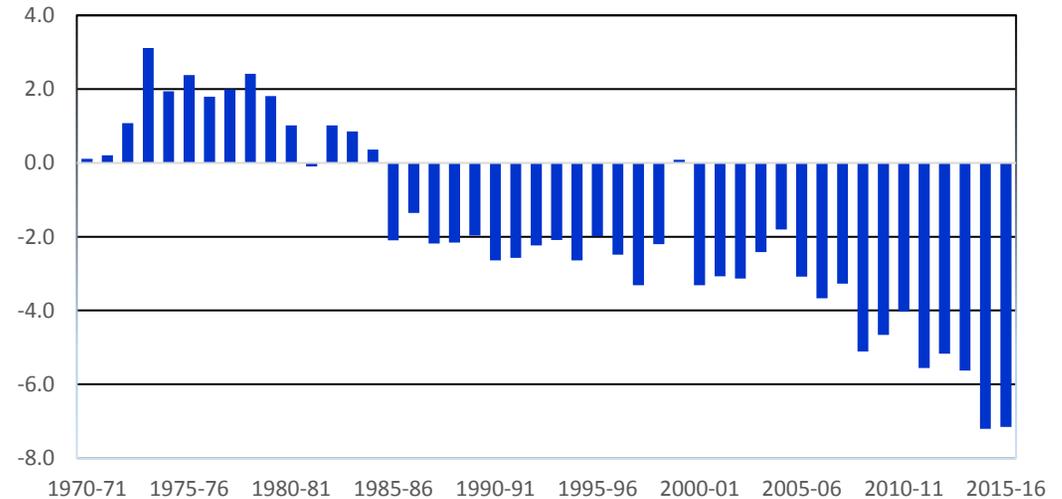


Figure 1 shows that as a result of the asymmetric fiscal responses to resource revenue fluctuations, there has been a cumulative reduction of \$7,153 per capita in Alberta's net financial assets since 1970-1971. This corresponds to an increase in the province's net debt of \$30.4 billion in 2017 dollars.

To break out of this cycle and avoid further accumulations of debt, the provincial government should put unanticipated increases in resource revenue in a fiscal stabilization fund, or the Alberta Heritage Savings Fund, rather than increase spending in the short term.