



Capital Borrowing Policy: A Smart Debt Ceiling

Issue

Provincial infrastructure underpins Alberta's economy, and is critical to the province's ability to efficiently provide services, transport people and goods, and enhance productivity. Lack of investment has created an infrastructure debt estimated at \$7 billion in 2005.¹

Calgary Chamber of Commerce Position

A number of factors have aligned to make debt financing of major infrastructure projects an attractive option for the province:

- Alberta is considered a safe place for investment with its AAA credit rating.
- The economic slowdown has forced central banks to lower both short and long term interest rates to low levels.
- The province holds a significant amount of capital in its various savings vehicles, with the potential to earn a rate of return greater than the rates the province would be charged on infrastructure-related loans.
- The cancellation and delay of many large private projects has loosened the market for both labour and goods, thus decreasing the total cost of construction.

Though the term 'debt' has a particularly negative connotation in Alberta, there are times when debt is a wise choice. By investing during a period of slow growth the province can mitigate the worst of the economic slowdown by providing jobs to workers and income to businesses, while positioning to reap the benefits of infrastructure investment.

'Smart debt' is a valid form of infrastructure financing but should only be used in conjunction with a few broad parameters on how and when to borrow, namely:

- Only a few capital projects are well-suited for tax-supported debt financing. These include large one-time projects with long asset lives that can leverage additional financing elsewhere (e.g. water pipelines, sewer and roads, etc). Operational intensive projects such as hospitals and schools are not suitable candidates for debt financing.
- Smart debt programs require a definition of a sustainable level of borrowing or some notion of optimal debt relative to future revenues and anticipated growth – to prevent unsustainable and out of control borrowing.
- Pursuing smart debt policies requires setting out guidelines regarding debt structure and amortization – projects should be financed over the useful life of the asset rather than based on arbitrary time lines or lowest cost financing.
- Smart debt plans recognize that debt only finances infrastructure, and that the debt must be funded. Before issuing debt, the province must draw up a comprehensive repayment plan.

¹Government of Alberta 2008. 20-Year Strategic Capital Plan.

5 MINUTE POLICY BRIEFS



Policy Recommendations

The Calgary Chamber of Commerce recommends that the Government of Alberta:

1. Includes an exhaustive list of large, one-time capital projects (such as water infrastructure, roads, bridges etc.) as candidate projects for debt financing.
2. Establishes a *Smart Debt Ceiling* whereby total capital debt servicing costs are capped at 0.5 per cent of total provincial revenues (based on a three year moving average).
3. Sets amortization terms over the useful life of the debt financed assets – to ensure the beneficiaries (i.e. current and future Albertans) share the costs.
4. Establishes a comprehensive repayment plan, with a focus on ensuring the province's accumulated debt, as estimated in its long-term capital plan, not exceed the *Smart Debt Ceiling*.