

## Economics

# PROVINCIAL BUDGET BRIEFS

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## British Columbia budget 2023

The strong economic recovery seen in British Columbia to date, combined with the impact of inflation on tax revenues, means that the province is expecting to post a second consecutive surplus in the outgoing fiscal year. However, the \$3.6bn surplus now projected is lower than the mid-year update, due to new spending announced since that time. Increased spending on health and affordability will also continue into fiscal 2023/24 and, when combined with conservative forecasts for tax revenue in a slowing economy, results in the province projecting a \$4.2bn deficit (approximately 1% of GDP). The return to operating deficits, combined with a notable increase in capital spending plans, sees borrowing requirements jump from \$8.9bn in the current fiscal year to \$19.0bn in fiscal 2023/24.

Table 1: Summary of fiscal position: (C\$billions)

| Fiscal measure                  | 2021/22<br>Actual | 2022/23<br>22 Budget | 2022/23<br>23 Budget | 2022/23<br>Change | 2023/24<br>23 Budget | 2024/25<br>23 Budget | 2025/26<br>23 Budget |
|---------------------------------|-------------------|----------------------|----------------------|-------------------|----------------------|----------------------|----------------------|
| <b>Revenue</b>                  | 72.392            | 68.552               | 82.700               | 14.148            | 77.690               | 79.724               | 82.223               |
| Own Source                      | 60.412            | 57.212               | 70.215               | 13.003            | 64.097               | 66.540               | 68.742               |
| • % change                      | 22.6              | -2.6                 | 16.2                 | 18.8              | -8.7                 | 3.8                  | 3.3                  |
| Federal transfers               | 11.980            | 11.340               | 12.485               | 1.145             | 13.593               | 13.184               | 13.481               |
| <b>Expenditures</b>             | 71.086            | 71.013               | 74.393               | 3.380             | 80.206               | 82.978               | 84.766               |
| Program spending                | 68.344            | 68.087               | 71.534               | 3.447             | 76.971               | 79.264               | 80.617               |
| • % change                      | 5.3               | 6.8                  | 4.7                  | -2.1              | 7.6                  | 3.0                  | 1.7                  |
| Public debt interest            | 2.742             | 2.926                | 2.859                | -0.067            | 3.235                | 3.714                | 4.149                |
| Pandemic recovery contingencies | 0.000             | 2.000                | 2.000                | 0.000             | 1.000                | 0.000                | 0.000                |
| Supplementary estimates         | 0.000             | 0.000                | 2.715                | 2.715             | 0.000                | 0.000                | 0.000                |
| Forecast allowance              | 0.000             | 1.000                | 0.000                | -1.000            | 0.700                | 0.500                | 0.500                |
| <b>Surplus /(deficit)</b>       | 1.306             | -5.461               | 3.592                | 9.053             | -4.216               | -3.754               | -3.043               |

## BC economy expected to stumble, but not tumble, in 2023

Relative to other provinces, the BC economy saw one of the shallowest declines in activity during 2020, and one of the strongest recoveries in 2021 and 2022. However, higher interest rates are expected to bite this year, with the province projecting only limited growth in real GDP of 0.4% in 2023. The 1.5% growth rate anticipated for 2024 would also be below the pace of population growth (anticipated at 1.9%), and therefore represent a modest decline in per-capita terms. The sluggish patch for GDP is expected to see the unemployment rate rise to 5.7%, after averaging 4.6% in 2022, while also seeing corporate profits decline in both 2023 and 2024. These forecasts factor into the province's projections for lower corporate and personal income tax receipts ahead.

The province's forecasts show a decline in interest rates in 2024, with the three-month bond yield falling from 4.16% in 2023 to 3.16% next year before stabilising around 2.5% by the end of the forecast horizon. The Government of Canada 10-year yield is expected to stabilise at around 2.75% in the outer years of the projections.

Table 2: Key assumptions (Y/Y % chg)

| Economic assumptions     | 2022 | 2023  | 2024 | 2025-27 |
|--------------------------|------|-------|------|---------|
| Real GDP                 | 2.8  | 0.4   | 1.5  | 2.3     |
| • Private sector average | 3.0  | 0.5   | 1.6  | 2.2     |
| Nominal GDP              | 11.0 | 2.8   | 3.7  | 4.2     |
| Employment               | 3.2  | 0.4   | 1.0  | 1.1     |
| Unemployment rate (%)    | 4.6  | 5.7   | 5.6  | 5.2     |
| Retail sales             | 3.0  | 1.8   | 2.9  | 3.5     |
| Housing starts (K)       | 46.7 | 39.0  | 37.0 | 38.0    |
| Personal income          | 7.1  | 6.1   | 4.3  | 4.0     |
| Corporate profits        | 13.5 | -14.5 | -7.0 | 4.1     |
| CPI                      | 6.9  | 3.9   | 2.5  | 2.1     |
| Population               | 2.2  | 2.4   | 1.9  | 1.6     |

Table 3: Key financial assumptions

| Financial assumptions (fiscal yr) | 2022 | 2023 | 2024 | 2025-27 |
|-----------------------------------|------|------|------|---------|
| 3-month T-Bills (%)               | 2.30 | 4.16 | 3.16 | 2.54    |
| 10-year GoC Bonds (%)             | 2.77 | 3.01 | 2.90 | 2.75    |
| Exchange rate (US\$/C\$)          | 76.8 | 74.7 | 77.4 | 78.7    |

Table 4: Commodity assumptions

| Commodity assumptions | 2022/23 | 2023/24 | 2024/25 | 2025/26 |
|-----------------------|---------|---------|---------|---------|
| Stumpage rate (\$/cm) | 36.2    | 18.1    | 19.0    | 21.8    |

Note: 2025-27 is a three-year average

## A return to deficits expected

For the outgoing 2022/23 fiscal year, the province now expects to see a surplus of \$3.6bn. While that is quite a difference relative to the Budget 2022 forecast for a \$5.5bn deficit, it is a modest deterioration relative to the mid-year update (\$5.7bn surplus). Tax revenues continue to surprise to the upside thanks to the strong economic recovery and inflationary pressures impacting nominal receipts. Total revenues are running \$1.6bn higher than at the time of the mid-year update and \$14.0bn above what was anticipated at the time of last year's budget.

However, the province has also added to spending. Since the mid-year update, and including measures announced today, spending is running \$4.0bn higher. Of that, \$2.7bn represents supplementary estimates awaiting legislative approval to fund supports for local governments with the costs of upgrading infrastructure, ferry fare affordability among other areas. There were also \$500mn additions to both the Rental Protection Fund and the BC Affordability Credit, the latter of which enhances the April payment for the Climate Action Tax Credit.

For the upcoming 2023/24 fiscal year, a return to deficit is anticipated. That partly reflects forecasts for a weaker economy that translates into lower taxation revenue, particularly for personal income and corporation tax. Overall, own-source revenue is projected to be roughly \$6.0bn lower in 2023/24 than in the outgoing fiscal year. However, the province is also increasing spending, particularly in areas related to health and affordability. Affordability measures include the creation of a renters' tax credit, increases in the BC Family Benefit, as well as funding for free prescription contraception.

The \$4.2bn deficit projected for fiscal 2023/24 is around 1% of provincial GDP. As is common practice in BC, that projection includes a number of contingencies. A \$700mn forecast allowance allows for some slippage in revenues in case of a worse economic outcome. A contingencies vote allowance totalling \$5.5bn in fiscal 2023/24 allows for spending related to pandemic recovery funding, agreements under the Shared Recovery Mandate, costs related to climate change and CleanBC.

The medium term projections show the pace of spending growth slowing, while revenues start to recover following the decline anticipated for the upcoming fiscal year. Because of that, the deficit is anticipated to be a simmer \$3.8bn in 2024/25 and \$3.0bn in 2025/26.

## Gross borrowing requirements to jump higher on deficit and capital spending

As we have been seeing from the latest provincial updates, the outgoing fiscal year ending March 31, 2023 shows a much stronger year than originally planned. That is also the case with British Columbia, as the gross borrowing requirements for 2023/23 have dropped substantially from initial estimates due to improved finances. As of today, the province is forecasting \$8.9bn of gross requirements, down from \$19.0bn originally. Of that total requirement, \$500mn still remains to be funded this year. However, the province did not specify if it would be completed through short-term or long-term funding.

Considering the province borrowed \$4.0bn in the domestic market through eight syndicated deals this year, with each transaction consisting of \$500mn lots, it wouldn't be too far of a stretch to assume the remaining requirements will be completed by a long-term debt transaction. The other deal completed this year was a €100mn transaction, which was the province's only international deal. That is much lower than prior years, as non-domestic issuance represented roughly 35% of the province's entire issuance in 2021/22. Due to higher upcoming borrowing requirements, we suspect a larger portion of international issuance will be completed going forward.

As for this upcoming fiscal year, the gross borrowing requirements are expected to increase by \$10.2bn to \$19.0bn, almost the identical figure to that which was originally forecasted for 2022/23. The increase is a result of the province returning to a deficit forecast of \$4.2bn relative to the surplus of \$3.6bn in the outgoing year, while capital spending jumps up by \$3.7bn to \$15.8bn. Overall, the three-year fiscal plan sees gross borrowing remain elevated due to higher capital requirements and deficit forecasts, with estimates of \$20.5bn in 2024/25 and \$19.3bn in 2025/26.

Total capital spending is expected to be \$48.5bn over the three-year plan with focus on areas related to schools, post-secondary facilities, hospitals, roads, bridges, and other infrastructure projects around the province. Over 75% of that total is taxpayer-supported capital spending, expected to be around \$37.5bn. That is some \$10.0bn higher than Budget 2022, mainly due to the progression of major infrastructure projects, increased housing investments, as well as additional funding for maintenance and upgrades of existing government assets.

Table 5: Borrowing requirements (C\$billions)

| Borrowing requirements                    | 2022/23<br>Estimate | 2023/24<br>Forecast | 2024/25<br>Forecast | 2025/26<br>Forecast |
|-------------------------------------------|---------------------|---------------------|---------------------|---------------------|
| Operating deficit /(surplus) <sup>1</sup> | -3.592              | 4.216               | 3.754               | 3.043               |
| Capital investment / requirements         | 12.172              | 15.840              | 16.750              | 16.951              |
| Other financing sources <sup>2</sup>      | -3.990              | -4.642              | -4.025              | -6.780              |
| <b>Net financial requirements</b>         | <b>4.590</b>        | <b>15.414</b>       | <b>16.479</b>       | <b>13.214</b>       |
| Maturities and calls                      | 4.295               | 3.632               | 3.975               | 6.170               |
| <b>Total gross</b>                        | <b>8.885</b>        | <b>19.046</b>       | <b>20.454</b>       | <b>19.384</b>       |

Table 6 Sources of funding (C\$billions)

| Sources of funding            | 2022/23<br>Estimate | 2023/24<br>Forecast | 2024/25<br>Forecast | 2025/26<br>Forecast |
|-------------------------------|---------------------|---------------------|---------------------|---------------------|
| Internal sources/ST borrowing | 4.481               | 0.000               | 0.000               | 0.000               |
| Bonds and MTNs                | 4.404               | 19.046              | 20.454              | 19.384              |
| <b>Total</b>                  | <b>8.885</b>        | <b>19.046</b>       | <b>20.454</b>       | <b>19.384</b>       |

<sup>1</sup> Includes forecast allowances

<sup>2</sup> Includes other financing sources for the province, the health and education sectors, Crown corporations and adjustments for non-cash budgetary items.

## Debt to GDP ratio on the rise, but from a lower base

As a result of the lower gross borrowing requirements for this outgoing year, taxpayer-supported debt-to-GDP is expected to be 16.4%, down 3.6% from the budget estimate of 20.0%. For this upcoming fiscal year, that ratio is expected to increase by 2.5% to 18.9%. However, that ratio is still down 2.9% from last year's estimates due to the better hand-off. As gross borrowing requirements remain elevated, that ratio continues to trend upwards, reaching 23.0% by the end of the forecast horizon (i.e. 2025/26). Despite the upward trend, the province should still maintain one of the lower ratios amongst its provincial peers.

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