The Province of British Columbia’s NDP government continues to post budget surpluses while also spending on election commitments. For the nearly completed 2018/19 fiscal year, the $374mn surplus now expected is $155mn more than at the time of the previous budget, and still includes a $500mn forecast allowance. Higher personal income and corporate tax receipts have helped offset the impact that the housing market slowdown has had on property taxes, as well as a larger net loss related to the Insurance Corporation of British Columbia (ICBC). In 2019/20, the $274mn surplus projected includes $1.25bn in total fiscal prudence ($500mn forecast allowance plus a $750mn contingencies vote allowance to guard against unforeseen or unbudgeted costs). Capital spending will take a step up in 2019/20 to $10.6bn, increasing from an updated forecast of $9.0bn for 2018/19, contributing to gross borrowing requirements increasing in 2019/20 to $7.5bn, up from $6.8bn in 2018/19.

### Economic Growth: Cooler But Not Cold

Growth in the BC economy has cooled after a strong 2017, but the slowing hasn’t been worse than what was expected at the time of last year’s budget. GDP growth is expected to have been 2.2% in 2018, only a 0.1%-pt downgrade from that expected at Budget 2018. A cooling housing market, reflecting the combination of higher interest rates and tighter regulatory policy, has been a primary source of the slowing and has been mainly seen in lower resale activity. Housing starts, while falling from 2017, were actually higher in 2018 than had been expected a year ago.
Looking forward, the Province sees real GDP growth coming in slightly stronger than its previous forecasts in 2019 and beyond, owing largely to some trade uncertainty being lifted by the Canada-United States-Mexico Agreement (CUSMA) and the major LNG Canada project which would see stronger business investment than previous anticipated. However, the Ministry of Finance’s estimates of 2.4% real GDP growth in 2019, 2.3% in 2020, and averaging 2% beyond that, are on average 0.2%-pts below the average of private sector forecasters. Using slightly lower growth rates than the consensus adds a level of prudence to the fiscal plan. Housing starts are expected to continue falling towards levels more in keeping with those seen historically, easing to 34K in 2019 from almost 41K in 2018.

Modest Surplus Still Expected For Outgoing 2018/19...
Updated projections for the 2018/19 fiscal year continue to show the Province on track to post a larger surplus than initially expected, albeit a smaller one than at the time of the mid-year update. The $374mn surplus now expected compares to $219mn at the time of Budget 2018, and $1.35bn at the time of the mid-year update. Even though the fiscal year is drawing to a close, the surplus projected still includes $500mn in forecast allowance, which is actually $150mn more than at the time of last year’s budget. As such, the final surplus could well be higher.

Personal income tax receipts are running $1.5bn higher than what was initially anticipated in Budget 2018. Corporate income tax receipts are also $1.04bn higher, despite seeing a $269mn downgrade compared to the mid-year update and accounting for the impacts of Federal tax measures announced in the Fall Economic Statement. Due to the slowing housing market, property transfer taxes are set to bring in $325mn less than initially budgeted for.

The strength in tax revenue helped offset higher costs related to the wildfire fighting, with fire management costs ($551mn more than Budget 2018) and spending related to the Emergency Program Act ($308mn higher than Budget 2018) both coming in above previous expectations. Losses related to the Insurance Corporation of British Columbia are running $496mn higher than initially budgeted for, and in the latest update there was also a write-down related to BC Hydro. As a result of the joint Comprehensive Review of BC Hydro, the government accepted a recommendation that BC Hydro write off the balance of its Rate Smoothing Regulatory Account estimated at $1.136bn. The net negative impact on the 2018/19 fiscal outlook is $186mn, with a $950mn adjustment recognized in the 2017/18 fiscal year.

...and More to Come in 2019/20 and Beyond
The Province tabled another surplus for 2019/20, alongside some additional spending on commitments related to improving affordability, enhancing services and developing a greener economy. Budget 2019 fulfills the prior commitment to eliminate Medical Service Plan (MSP) premiums, and introduced the new BC Child Opportunity Benefit. That will provide families with children under 18 up to $1600 a year for the first child, up to $2600 a year for two children and $3400 a year for families with three children, effective from October 1st 2020. It is projected to
cost $125mn in 2020/21 and $250mn in 2021/22. The Province will also eliminate interest on BC student loans, at an aggregate cost of $318mn over four years, while Budget 2019 additionally includes $679mn over the fiscal plan for Clean BC initiatives.

Overall, a $274mn surplus is expected for 2019/20. That projection includes a $500mn forecast allowance, but also a $750mn contingencies vote allowance to guard against unforeseen or unbudgeted costs. That means total fiscal prudence amounts to $1.25bn for the coming fiscal year. While personal income tax and corporation tax receipts are projected to be lower in 2019/20 than the outgoing fiscal year, overall revenue is slated to be higher thanks largely to revenue from the employer health tax (introduced in Budget 2018) and higher net income from Crown corporations. That includes a smaller ICBC loss of $50mn in 2019/20, from $1.18bn in 2018/19.

The overall budget surplus is seen rising to $585mn by 2021/22, although the total fiscal prudence for that year is lower at $700mn ($300mn forecast allowance + $400mn contingencies vote allowance).

Capital Spending to Increase Over Three-Year Fiscal Plan

Capital spending will take a step up in 2019/20 to $10.6bn, increasing from an updated forecast of $9.0bn for 2018/19. The largest variances are an increase of $900mn in BC Transportation Financing Authority (BCTFA) and an increase of $1bn in Columbia River power projects, the latter attributable to a $991mn purchase (51% interest) of the Waneta Dam power expansion. However, this $991mn is a one-time purchase and capital spending will decrease to $14mn and 18mn the following two years. Helping offset these increases are a reduction of $900mn in spending on BC Hydro. Overall, spending over the three-year fiscal plan through 2021/22 will see a total of $31.1bn spent on capital projects with around half primarily for power generation and transmission projects. Of note, operating debt was eliminated in 2018/19 which allows for operating cash surplus to be fully directed towards funding capital spending.

Taxpayer supported capital spending is forecasted to be $6.3bn, up $1.6bn from 2018/19 and remain elevated throughout the plan horizon. Increases in health spending and BCTFA are seen to have the largest effect. The latter includes Transportation Investment Plan and Transportation Investment Corporation (TIC), which became a subsidiary of BCTFA effective April 1, 2018. Note, TIC was no longer classified as self-supporting effective September 1, 2017 due to the cancellation of tolls on the Port Mann Bridge.

BC Hydro’s projected capital spending is decreasing to $3.0bn in 2019/20, down from $3.9bn in 2018/19 and will remain around $3bn both years thereafter. Much of the hydro’s electrical systems were built in the 1960-80s and require upgrades, maintenance, as well as new infrastructure built to help facilitate BC’s growing population and economy. BC Hydro represents majority (close to 95%) of all self-supported debt in the province.

Total provincial debt (including forecast allowance) for 2019/20 is estimated to be $72.5bn, up from $67.9bn in 2018/19, and will continue to grow reaching $77.7bn and $82.4bn the following two fiscal years. Two-thirds of the increase is coming from taxpayer-supported debt which is expected to reach $54.0bn by 2021/22, up from $44.0bn in 2018/19.

The province projects net debt (as reported in its Statement of Financial Position) to be $46.3bn at the end of 2019/20, increasing from $43.6bn in 2018/19 (updated forecast). It is then projected to be $50.3bn the following year and then reach $54.0bn by the end of the three-year plan. Net debt-to-GDP is projected to be 15.0% in 2019/20, up two ticks from 2018/19, and then rise to 15.6% and 16.1% the following two years.
Borrowings to Increase in Fiscal 2019/20

Gross borrowing requirements are expected to increase in 2019/20 to $7.5bn, up from $6.8bn in 2018/19, and continue to grow over the three-year plan horizon reaching $8.6bn in 2021/22. Much of the increase is due to financing infrastructure spending and refinancing requirements. Note, gross borrowing for 2018/19 was revised lower by $1.1bn from budget 2018 due to reduced capital spending and refinancing requirements.

We believe today’s budget is relatively neutral from a credit perspective as the province continues to project small surpluses over the three-year horizon. However, with debt-to-revenue and debt-to-GDP metrics forecasted to rise modestly over the plan, an upgrade from DBRS will be unlikely in the near-term. The province is projecting its net debt-to-GDP to increase from 14.8% in 2018/19 to 16.1% in 2021/22. Meanwhile, DBRS projects its own adjusted Tax-Supported Debt/GDP to be closer to 17.3% at the end of 2018/19, inclusive of unfunded pension liabilities, which will likely be higher going forward. This is above the 10-15% range required for a triple-A rating under its criteria, with an upgrade predicated on being sustainably at the lower end of the range. DBRS is the only rating agency that does not have a AAA rating for the province.

Credit Implications: Neutral

Credit Ratings: DBRS AA (high), Moody’s Aaa, S&P AAA, Fitch AAA All Outlooks Stable

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