British Columbia Budget Highlights

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Highlights and analysis of British Columbia's FY18/19 budget February 20, 2018, 4:30 pm

Housing Battle Continues

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The Province of British Columbia is projecting a small $219 million surplus for FY18/19 (0.1% of GDP), which would mark the sixth consecutive year in the black. A $350 million forecast allowance is in place, along with $550 million for spending contingencies, providing plenty of wiggle room for the upcoming fiscal year—this prudence also rises to larger-than-normal levels through the forecast horizon. Case in point is a big unexpected loss at ICBC that carved $1.3 billion from the FY17/18 surplus. The FY17/18 shortfall is now pegged at $151 mln (versus $190 million most recently). Small surpluses extend over the three-year forecast horizon, but net debt has begun to rise moderately as a share of GDP, thanks to a hefty capital spending program. This is a noteworthy turnabout after the ratio fell almost 3 ppts in the four years through FY16/17. From a policy perspective, this budget builds on the fall update, which itself rolled out a number of measures, including higher spending, and higher personal, corporate and carbon taxes. Spending remains a priority in this document, with a focus on childcare and housing, paid for in part by a handful of tax increases totaling $2.1 billion by FY19/20. The new housing measures will grab headlines:

Summary of Major Housing Measures

- A 5 ppt **increase in the foreign buyers'** tax, to 20%, with an expansion to cover a broader geography (e.g., Victoria, Nanaimo, Fraser Valley and Kelowna).
- New **'speculation tax'** on nonresident owners of residential property, or satellite families that pay little or no domestic income tax. This will start at 0.5% of assessed value in 2018, rising to 2% in 2019. Some properties (i.e., long-term rentals) will be exempt up front, and a non-refundable income tax credit will be available.
- Crackdown in areas such as real estate **ownership by numbered companies** and **pre-sale condo assignments**.
- Increased **property transfer tax** on homes above $3 million, from 3% to 5%. Also, higher **school taxes** for most.
- $6 billion over 10-years for **affordable and rental housing**.

All told, B.C. is now applying the full-court press on housing affordability, pretty well pulling out all stops short of creating new land. These measures should help further dampen speculative psychology and build on the impact of higher interest rates and stricter OSFI rules. Note that Vancouver single-detached prices have been stable, while those on Vancouver Island and in the Fraser Valley are pushing new records—look for the latter markets to stall.

Table 1
Fiscal Summary

British Columbia (C$ mlns, except where noted)

	Est.	— Forecast —		
	17/18	18/19	19/20	20/21
Revenues	53,365	54,877	57,580	58,566
Expenditures	51,818	53,624	56,778	57,762
Forecast Allowance	(100)	(350)	(500)	(600)
Net ICBC impacts	(1,296)	(684)	(21)	80
Budget Balance	151	219	281	284
Taxpayer-Supported Debt	43,680	45,198	47,554	50,257
Total Provincial Debt	65,264	69,372	73,081	77,054
As a percent of GDP:				
Budget Balance	0.1	0.1	0.1	0.1
Taxpayer-Sup. Debt	15.6	15.5	15.7	15.9
As a percent of revenue:				
Resource Revenues	5.0	4.5	3.8	3.7
Federal Transfers	15.9	16.4	16.6	16.6
Key assumptions:				
Real GDP (% chng)	3.0	2.1	2.0	2.0
Nominal GDP (% chng)	4.7	4.0	3.9	3.9

Source: Provincial Budget ( ) = deficit
Note: GDP figures are for calendar year (FY18/19=CY18)

Table 2
Borrowing Requirements

British Columbia (C$ mlns)

	17/18	18/19	19/20
Operating (surplus)	(151)	(219)	(281)
Capital requirements	6,811	9,235	8,239
Refinancing	2,712	3,239	1,990
Other sources	(7,406)	(4,337)	(3,888)
Gross borrowing requirement	1,966	7,918	6,060

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Some Other Notable Measures

- Full **elimination of Medical Service Plan premiums** by 2020.
- **Employer heath (payroll) tax** of 1.95% introduced starting in 2019, phased in for businesses with payrolls in excess of $500,000, with the maximum rate hit at a payroll of $1.5 million. This will raise a hefty $1.9 billion by FY19/20.
- **Child care benefit** of up to $1,250 per month, phased out based on income level, as well as subsidies to reduce fees.

Prior Tax Increases Support Revenue

Total revenue is forecast to rise 4.0% to $54.9 billion in FY18/19, alongside higher personal income tax revenues (rates on both personal and corporate income were raised in the fall budget update, and net incremental tax increases were pegged at $305 million for FY18/19). Property transfer taxes (which account for roughly 4% of the total revenues) are expected to rise modestly. All told, net new **revenue measures** announced in this budget will rise to $2.1 billion by FY20/21, with the employer health tax driving most of the increase.

The revenue outlook is based on conservative **economic assumptions**, as is usually the case with B.C. Real GDP is projected to grow 2.3% in 2018 and 2.0% in 2019. That forecast is a safely below our call for growth of 2.5% and 2.1%, respectively, and would be down from a five-year average growth clip of more than 3.0%. Still, growth in British Columbia is likely to lead the country this year, and the province is coming off the strongest four-year average growth run since 2007. While labour market and consumer spending trends should remain solid, higher interest rates and ongoing efforts to cool housing activity will likely pull growth down toward its potential rate.

Spending Growth Firm

Total expenses are projected to rise 3.5% in FY18/19 to $53.6 billion, building on a late-year ramp up in FY17/18 that lifted full-year spending a hefty 6.4%. Health care will get a 4.5% boost, while education spending will rise at a 3.9% clip. Spending growth is projected to remain firm through FY19/20, before slowing down, with childcare and housing, as mentioned above, key priority areas. In a nutshell, we've seen a clear shift toward stronger spending growth in the province that doesn't appear to be tapering off anytime soon.

Meantime, **capital spending** will grow at a much stronger pace than program spending, jumping $2.4 billion to $9.2 billion in FY18/19 (combined taxpayer-supported and self-supported capex). It will then dip thereafter, with taxpayer-supported capex holding slightly over $5 billion per year. A wide range of sectors will see infrastructure investment boosted in FY18/19, with a number of the supply-side initiatives on the housing front flowing through the capital budget.

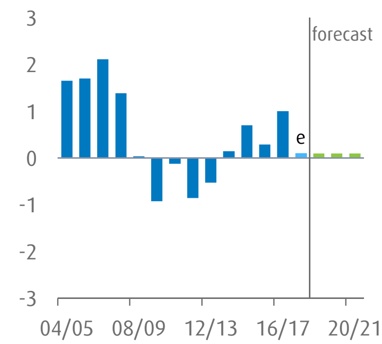
Debt Ratio Creeping Up Again

The combination of higher capital spending and a small budget surplus will lift taxpayer-support debt by $1.5 billion in FY18/19, to $45.1 billion, or 15.5% of GDP (down a tick from the current fiscal year). Overall **net**

Chart 1
Small Surpluses Persist

British Columbia (C$ blns)

Budget Balance

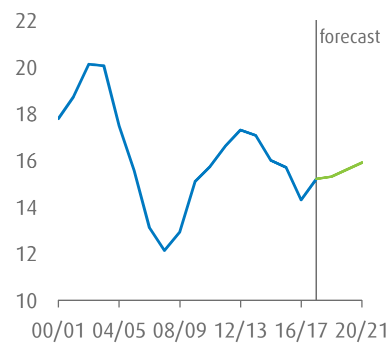


Source: Provincial Budget e = estimate

Chart 2
Debt Ratio Creeping Up

British Columbia (% of GDP)

Net Debt



Source: Provincial Budget

debt, however, is on the rise again and will inch up as a share of GDP, expected at 15.3% this year. That's down from a recent high of 17.1% six years ago, but the debt trajectory has clearly shifted from downward to flat. Indeed, ramped up spending in this budget (and the prior fall update), along with softer expected nominal GDP growth, will set most debt ratios on a modestly-upward track for the coming three fiscal years. While not as pleasing as seeing debt ratios fall year after year, the level remains highly favourable versus most of B.C.'s provincial peers and should keep the AAA credit intact for now—but the shift in priorities won't go unnoticed.

Gross **provincial borrowing** is estimated at $7.9 billion for FY18/19, up from $2.0 billion in FY17/18—the latter came in below expected due to lower capital spending. Borrowing then ebbs to average around $6.5 billion in FY19/20 and FY20/21.

The Bottom Line: The suite of housing measures will grab most of the attention in this budget, and rightfully so. Beyond that, however, is a noteworthy shift to bigger spending and creeping debt ratios again, in what is arguably the latter-stages of the economic cycle. To be sure, the moves on this front are subtle, and the fiscal plan is backed by thick contingencies, but it's probably safe to say that we've seen B.C.'s best days from a credit perspective for now.