



BRITISH COLUMBIA BUDGET 2017

February 22, 2017

Allocating the fiscal dividend

- The BC government projects budget surpluses of \$295 million in FY17/18 (a fifth consecutive surplus), \$244 million in FY18/19 and \$223 million in FY19/20.
- This follows an upwardly revised surplus of \$1.5 billion in FY16/17.
- A strong fiscal position going into Budget 2017 gave the BC government a hefty ‘fiscal dividend’ that it allocated to tax cuts and increased program spending.
- A host of measures reduces the tax burden by \$566 million in FY17/18 (and by a larger \$1.3 billion in FY18/19).
- There is additional spending on a number of core items, including education, health and affordable housing.
- The province’s taxpayer-supported debt is expected ease slightly as a share of GDP to 15.9% in FY17/18, still one of the lower ratios among the provinces.

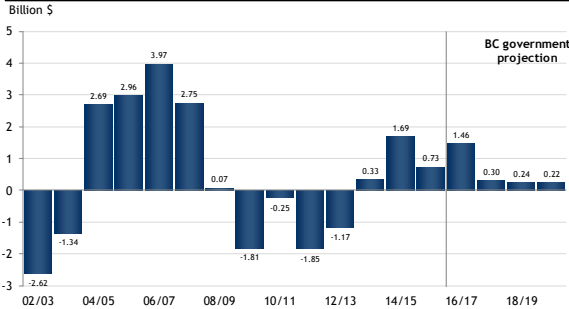
Facing Budget 2017 from a position of strength...

With a string of budget surpluses already under its belt in the previous four years, the BC government set out to prepare Budget 2017 from a position of strength. It was known from quarterly updates since Budget 2016 that the province’s fiscal picture had improved considerably in the past year, with the surplus for FY16/17 shaping up to be much larger than the \$264 million projected originally thanks to stronger-than-expected revenues. The latest update on FY16/17 delivered in Budget 2017 shows that total revenues for that year have been revised upwardly by an out-sized \$2.8 billion (5.9%). This revision dwarfed a boost of \$1.6 billion (3.4%) to the expense projection, such that the surplus climbed to \$1.5 billion, up by \$1.2 billion relative to Budget 2016. These updated projections offered a stronger starting point for the 2017 fiscal plan.

...with a desire to please the electorate

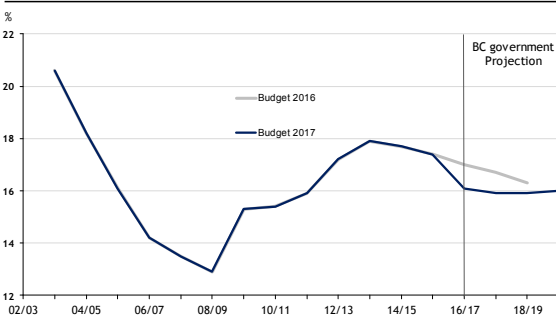
The increase in fiscal flexibility came at an opportune time for the governing BC Liberals as they prepare for provincial elections in the spring. It provides them with the means in Budget 2017 to shift focus from fiscal restraint—earlier necessary to re-balance the books on a sustained basis—to advance other policy items while maintaining fiscal discipline. Indeed the budget presented yesterday charted a course that included both a host of tax reductions and increased spending over the three-year fiscal plan. British Columbians will cast their ballots to elect their next government on May 9.

British Columbia's budget balance



Source: British Columbia Ministry of Finance, RBC Economics Research

Tax-payer supported debt to GDP ratio - BC



Source: British Columbia Ministry of Finance, RBC Economics Research

Budget assumptions

	2016	2017	2018	2019
Real GDP growth (%)				
Budget 2017 planning assumption	3.0	2.1	2.1	2.0
RBC	3.3	1.7	1.8	
Private sector average*	3.1	2.3	2.2	2.1
Nominal GDP growth (%)				
Budget 2017 planning assumption	4.7	4.1	4.0	3.9
RBC	4.9	3.7	3.9	
Private sector average*	4.8	4.3	4.1	4.0

* BC Economic Forecast Council survey (updated January 2017)
Source: BC Ministry of Finance, RBC Economics Research

Robert Hogue
Senior Economist
(416) 974-6192
robert.hogue@rbc.com

Some things don't change: fiscal discipline...

While the course charted in Budget 2017 signals a shift in focus, fiscal discipline remains a priority. The BC government projects a surplus of \$295 million in FY17/18, which would constitute a fifth consecutive surplus. Further surpluses of \$244 million in FY18/19 and \$223 million in FY19/20 are projected for the remaining two years of the fiscal plan.

....and prudence

As per usual practice, economic assumptions underlying the budget are conservative. For the purpose of budget projections, the BC government uses a real GDP growth forecast of 2.1% for both 2017 and 2018, which is 0.2 percentage points below the average from private sector forecasters. These growth rates are slightly stronger than RBC Economics' 1.7% in 2017 and 1.8% in 2018 but not exceedingly so. Forecast allowances of \$350 million in FY17/18 and \$250 million in each of the following two years provide a further measure of prudence.

Other things do: several new tax measures...

Last week's Throne Speech indicated the government's intention to give money back to British Columbians and yesterday's budget offered several tax measures that put more money into the pockets of British Columbians—to the tune of \$566 million in FY17/18 and rising to \$1.3 billion in FY18/19. Chief among these measures is a 50% reduction in Medical Services Plan premiums for household with annual income of less than \$120,000 that will take effect on January 1, 2018—which will cost the government \$211 million in FY17/18 and \$845 million in FY18/19. The government indicated that this reduction is a first step toward eliminating those premiums entirely when it “becomes affordable”, although no timeline was provided. There were a number of smaller tax measures including a reduction in the small business tax rate (costing \$68 million in FY17/18), an increase in the threshold for the home owner grant (\$48 million), and the phasing out of the provincial sales tax on electricity (\$41 million).

...and expenditure increases

Budget 2017 sees a spending boost to a number of programs, including \$740 million over three years to education, \$796 million over three years to support families, individuals and children in need, \$100 million over three years to support services addressing mental health and substance use issues, and \$65 million over two years to create more housing units for people with mental health and substance abuse issues. In the fall of 2016, the BC government had announced a \$500 million increase over five years to create 2,900 affordable housing units in partnership with other organizations and local governments.

Flat revenues and modest rise in expenditures in FY17/18

Overall government revenues are projected to be \$50.8 billion in FY17/18, down marginally by 0.1% compared to FY16/17, with modest increases in federal transfers and contributions from crown corporations more than offset by slight declines in revenues from taxation, natural resources and other sources. Revenue from the province's carbon tax is projected to be little changed at \$1.2 billion, and revenue from property transfer is projected to drop from a record \$2.0 billion in FY16/17 to \$1.5 billion in FY17/18. Government expenses are projected to rise by 2.3% to \$50.2 billion in FY17/18. Program expenditures are slated increase by 2.1% and debt servicing costs by 5.3%.

Capital spending to get a significant boost

Spending increases are more substantial in the province's capital investment plan. Taxpayer-supported capital spending is projected to increase by almost \$700 million (16.5%) to \$4.8 billion in FY17/18, and total \$13.7 billion over the entire three-year fiscal plan. This latter figure represents a \$1.6 billion boost relative to the capital investment plan presented in Budget 2016. The BC Transportation Financing Authority (receiving an additional \$403 million) and education (\$354 million) will account for the entire increase in FY17/18. In addition to this investment done by taxpayer-supported entities, self-supported entities (crown corporations) also will boost their capital investment materially in the province by \$424 million (14.9%) to \$3.3 billion in FY17/18, and to a total of \$10.8 billion over the three-year plan.

Provincial debt under control

The taxpayer-supported debt profile was increased marginally relative to Budget 2016. Taxpayer-supported debt is projected to rise from \$42.0 billion in FY16/17 (16.1% of GDP) to \$47.2 billion by FY19/20 (16.0% of GDP). The government notes that the portion of the debt that is direct operating debt will diminish progressively from \$5.2 billion in FY16/17 to \$1.1 billion by FY19/20—the lowest level since FY82/83.

Borrowing requirements to rise

The BC government borrowing requirements are scheduled to jump from \$3.2 billion in FY16/17 to \$5.8 billion in FY17/18. A further increase is expected in FY18/19 to \$7.6 billion before easing to \$7.4 billion in FY19/20. The total borrowing required over the fiscal plan (\$20.9 billion) will comprise of \$9.5 billion to fund taxpayer-support capital investments, \$6.7 billion to fund self-supported capital investments and \$4.7 billion to refinance existing debt maturities. The government also notes that it plans to retire

\$5.2 billion maturing debt over the fiscal plan, including \$2.4 billion in FY17/18.

Budget 2017 offers little bit of everything

With oil producing provinces facing significant fiscal challenges in the past couple of years, British Columbia has risen to the head of the class fiscally in Canada thanks to strict fiscal discipline, and a strong and diversified economy. With a fiscal dividend at hand going into Budget 2017, the BC government was in an envious position to ease off on budget restraint and tackle a number of priority items, including targeted tax breaks and spending increases. In the event, it did all of the above without jeopardizing its strong fiscal position. Whether the specific combination of tax breaks and spending increases announced in Budget 2017 is the right one will be up to British Columbians to decide on May 9.

British Columbia's fiscal plan

\$ billions	Actual	Forecast	Estimate	Plan	Plan
	<u>15/16</u>	<u>16/17</u>	<u>17/18</u>	<u>18/19</u>	<u>19/20</u>
Total revenues	47.6	50.9	50.8	51.2	52.0
Total expenses	46.9	49.1	50.2	50.7	51.6
Program spending	44.1	46.6	47.5	48.0	48.7
Interest on public debt	2.8	2.5	2.7	2.8	2.9
Surplus (before forecast allowance)	0.730	1.808	0.645	0.494	0.473
Forecast allowance		-0.350	-0.350	-0.250	-0.250
Surplus	0.730	1.458	0.295	0.244	0.223

The material contained in this report is the property of Royal Bank of Canada and may not be reproduced in any way, in whole or in part, without express authorization of the copyright holder in writing. The statements and statistics contained herein have been prepared by RBC Economics Research based on information from sources considered to be reliable. We make no representation or warranty, express or implied, as to its accuracy or completeness. This publication is for the information of investors and business persons and does not constitute an offer to sell or a solicitation to buy securities.

