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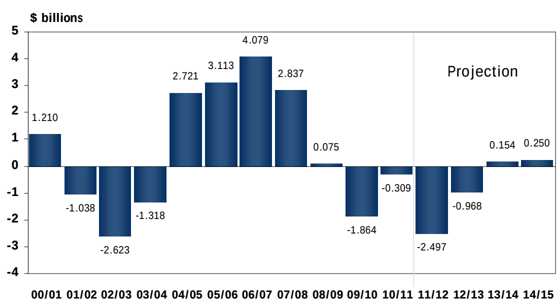
# B.C. BUDGET 2012

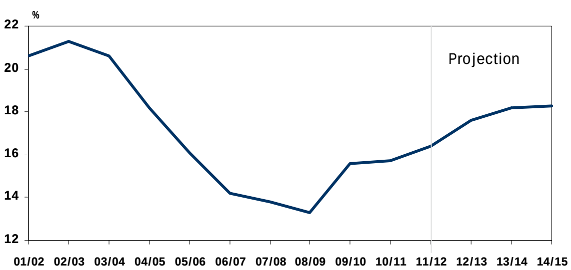
February 22, 2012

**British Columbia budget balance**




Source: British Columbia Ministry of Finance, RBC Economics Research

**Taxpayer-supported debt-to-GDP ratio**




Source: British Columbia Ministry of Finance, RBC Economics Research

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## Looking for stability

Following an eventful year on the B.C. fiscal scene in 2011 — during which the February 2011 budget was revised and tabled again in May under new B.C Finance Minister Kevin Falcon (and new Premier Christy Clark), British Columbians voted to 'extinguish' the HST in a referendum in August and the deficit estimate for 2011/12 ballooned — it is not surprising that the theme for Budget 2012 is *stability*. Yesterday, the B.C. government presented its latest fiscal plan that strives hard to stabilize spending in the next three years in order to eliminate the province's deficit by 2013/14, as required by law.

The provincial deficit is projected to total $970 million in 2012/13 (more than double the earlier projection of $440 million). According to the fiscal plan, this will be the fourth consecutive and last deficit of this cycle. The government projects surpluses of $154 million in 2013/14 and $250 million in 2014/15.

For the fiscal year ending March 31, the deficit is now estimated at $2.5 billion, significantly lower than the $3.1 billion in the November mid-year update but much higher than the $925 million projection in last year's budget (as revised in May). The jump in the deficit in 2011/12 relative to Budget 2011 primarily reflects the refund to the federal government of the $1.6 billion HST transitional assistance that the province received for the 2010 harmonization of its provincial sales tax with the GST.

The $594 million improvement relative to the November update is owed to the removal of most of the forecast allowance ($300 million), upwardly revised revenues ($101 million) and downwardly revised expenses ($193 million).

### Budget highlights

In this budget exercise, the B.C. government faced tough challenges in its deficit elimination pursuit by the prescribed timeline of 2013/14. In particular, the return to the old PST on April 1, 2013 — with its smaller tax base than the HST and the just announced $111 million transition relief for the housing industry — as well as slower expected economic growth dimmed its revenue outlook. This threatened to widen the gap with expenses. In response, the government introduced a number of measures aimed at ensuring that revenues will grow faster than expenses in its three-year fiscal plan.

The **measures** include:

- the continuation of the small business income tax rate at 2.5% (it was set to drop to zero on April 1, 2012) — this will bring in $281 million in extra revenue in 2012/13 and $261 million in 2013/14 ;

- a one percentage point increase in the corporate income tax rate to 11% on April 1, 2014 — $49 million in 2013/14 — however, this is a provisional measure which may be cancelled if economic growth is faster than expected; and

- the 'release' (sale) of surplus government assets by 2014 (which have yet to be identified) — $475 million in 2013/14.

- On the spending side, the B.C. government intends to maintain in the next three years its average expense growth target of 2.0% per year set in last year's budget.

The B.C. government is still working on the **PST transitional rules** for a wide variety of transactions. However, last week, it announced detailed rules applying to new housing. The announcement included new relief measures for purchasers and builders. Among them is the increase on April 1 of this year of the HST rebate threshold for new housing from $525,000 to $850,000, as well as the extension to secondary and recreational residences in regions other than the Vancouver and Victoria areas.

**Total revenues** are projected to rise 2.8% in 2012/13 to $43.1 billion. Own-source revenues (taxes, fees and crown corporation revenues) are expected to increase 4.6% to $35.8 billion, including a 22% ($212 million) rise in carbon tax revenues. On the other hand, federal transfers are set to fall 5.3% to $7.3 billion, reflecting drops in HST transition payments and other federal transfers. Total revenue growth is projected to accelerate to 3.5% in 2013/14, with the sale of surplus assets generating extra cash and federal transfers picking up again, before slowing even more to 2.5% in 2014/15. Over the entire three-year fiscal plan, the B.C. government expects total revenues to average a growth rate of 2.9%.

**Program expenditures** are planned to fall by 1.5% to $41.4 billion, from $42.0 billion in 2011/12. However, this decrease is due entirely to the one-time $1.6 billion HST refund to Ottawa in 2011/12, which will no longer be an expense in 2012/13. (While the refund is booked as an expense entirely in 2011/12, the actual transfer of cash will be done over five annual instalments starting in March 2012.) Excluding the effect of this payment, program expenditures are planned to increase by 2.4% in 2012/13. Program expenditure growth will slow substantially in the following years, to 0.5% in 2013/14 and 1.6% in 2014/15. As part of its plan to control program spending, the government is planning for declines of 2.7% per year in government employment (accomplished through attrition) and is extending its "net zero" wage increase policy governing collective agreements. **Total expenses** — including debt charges — are projected to decline 1.2% to $43.9 billion in 2012/13, and increase by 0.8% in 2013/14 and 2.1% in 2014/15. Excluding refundable tax credit transfers, which have been the object of an accounting change, the government says that the average expense increase of 2.0% per year during the three-year plan will represent a significant slowing from the average growth of 5.9% in the four years prior to the recession and 3.0% in the period since then.

**Taxpayer-supported capital spending** is projected to fall 6.0% to $3.8 billion in 2012/13, primarily reflecting the end of spending on the B.C. Place redevelopment, which will remove nearly $250 million from the books. With self-supported capital expenditures by provincial crown corporations scheduled to rise by 6.4% to $3.3 billion, total capital spending by provincial public entities is expected to be little changed, easing 0.5% to $7.1 billion. Total capital spending is slated to drop much more substantially by 15% to $6.0 billion in 2013/14 (due in large part to the scheduled completion of the Port Mann-Highway 1 project) and remain flat at that level in 2014/15.

**Taxpayer-supported debt** is projected to rise from $34.8 billion (16.4% of nominal GDP) in 2011/12 to $43.7 billion (18.3% of GDP) by 2014/15. **Total provincial debt**, which includes commercial crown self-supported debt, will grow from $51.0 billion in 2011/12 (24.1% of GDP) to $66.3 billion in 2014/15 (27.8% of GDP).

The B.C. government expects to **borrow $8.4 billion** and retire $2.2 billion worth of debt in 2012/13. For the entire three-year plan, the province anticipates total borrowings of $23.6 billion and retirements of $8.5 billion in maturing debt. Direct borrowing by Crown corporations and agencies are scheduled to be $291 million in 2012/13, down significantly from $609 million in 2011-12.

**Conservative assumptions and prudence will provide some protection**

As usual, assumptions imbedded in the fiscal plan presented yesterday were conservative. The B.C. government assumes real GDP growth rates of 1.8% in 2012 and 2.2% in 2013 for the province, which are weaker than our own forecasted rates of 2.3% and 2.5%, respectively. The government's assumptions for natural gas prices (a key factor underlying revenue estimates) also appear to be reasonably cautious at C$2.52/GJ for 2012/13 and C$3.04/GJ in 2013/14 — both revised substantially lower from previous forecasts. In addition to using a conservative basis for revenue projection, the plan maintains the two extra layers of prudence: a forecast allowance, which will rise from $200 million in 2012/13 to $350 million in 2014/15; and contingencies totalling $300 million in 2012/13 and $250 million in both 2013/14 and 2014/15.

With the main element of fiscal uncertainty last year — the fate of the HST — now known and the HST refund's one-time hit to B.C.'s bottom line booked in 2011/12, the top remaining challenge for the provincial government will be to stay on its ambitious spending restraint targets. The prudence shown by Minister Falcon in yesterday's budget, however, should normally provide enough protection against minor slippage on the expenditure front to ensure the elimination of the deficit by 2013/14.

**British Columbia's fiscal plan**

| $ billions | Actual | Forecast | Estimate | Plan | Plan |
|---|---|---|---|---|---|
| | **10/11** | **11/12** | **12/13** | **13/14** | **14/15** |
| **Revenue** | 39.9 | 41.9 | 43.1 | 44.6 | 45.7 |
| **Expense** | 40.2 | 44.4 | 43.9 | 44.2 | 45.1 |
| **Surplus (before fcst allowance)** | -0.309 | -2.447 | -0.768 | 0.404 | 0.600 |
| **Forecast allowance** | 0 | -0.050 | -0.200 | -0.250 | -0.350 |
| **Surplus** | -0.309 | -2.497 | -0.968 | 0.154 | 0.250 |
| **Total capital spending** | 6.6 | 7.1 | 7.1 | 6.0 | 6.0 |