

BRITISH COLUMBIA BUDGET 2017 UPDATE

September 12, 2017

More than a regular update

- The budget 2017 update is the first glimpse of the economic agenda of the province's new NDP government after 16 years of Liberal administrations.
- Expenditures get a big boost with more money spent on priority areas such as education, social assistance, housing and the elimination of bridge tolls.
- A strong provincial economy lays a solid foundation for this spending to occur.
- Targeted tax increases (personal income tax rate for higher-income individuals, general corporate income tax rate, carbon tax) further support the government spending plan.
- There are some targeted tax cuts (Medical Services Plan premiums, reduction of small business corporate income tax rate).
- The bottom line is little changed relative to the February 2017 budget. Small surpluses are projected throughout the three-year fiscal plan: \$246 million in FY17/18, \$228 million in FY18/19 and \$257 million in FY19/20.
- The province's taxpayer-supported debt is revised slightly higher by \$1.4 billion this year to \$44.9 billion due to a one-time adjustment. As a share of GDP, taxpayer-supported debt is expected to be 16.2% at the end of FY17/18, still one of the lower ratios among the provinces.

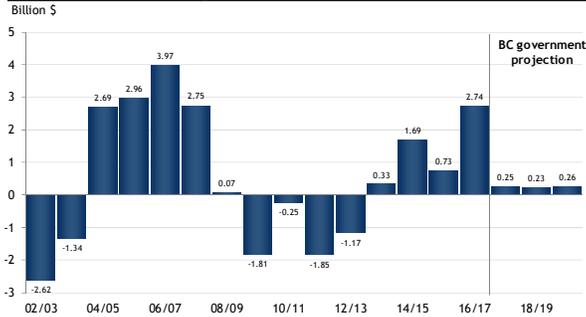
New government, new priorities,...

The eagerly-awaited update to the 2017 budget crafted by the previous Liberal government offered a first glimpse at the shift in direction that the 8-week old NDP government promises to deliver with the support of the Green Party. In this respect, this update packs more than a regular mid-year review. It offers significant revenue and expenditure measures to get the ball rolling on key themes the new NDP government campaigned on—improving affordability, enhancing services and providing economic opportunities for everyone. It contains a bit of everything: more spending, targeted tax hikes and targeted tax cuts.

...new approach...

The budget update also signals a new approach in some key areas. In particular, the new government ditches the tax neutrality of the provincial carbon tax. Going forward, future increases in the carbon tax—starting with a new \$5 per tonne rise schedule for April 1, 2018—will no longer need to be matched by an equal-sized tax cut somewhere else as has been the long-standing policy in British Columbia.

British Columbia's budget balance



Source: British Columbia Ministry of Finance, RBC Economics Research

Budget assumptions

	2016	2017	2018	2019
Real GDP growth (%)				
Budget 2017 Update	3.6	2.9	2.1	2.0
RBC	3.6	3.2	2.0	
Private sector average*	3.7	3.0	2.3	2.2
Nominal GDP growth (%)				
Budget 2017 Update	5.1	5.1	4.1	4.0
RBC	5.1	5.6	3.8	
Private sector average*	5.1	5.3	4.3	4.2

* BC Economic Forecast Council survey (updated September 2017)

Source: BC Ministry of Finance, RBC Economics Research

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...but still staying within the province's means

Yet, other than a few marquis measures, the budget 2017 update didn't represent a change in fiscal philosophy from the previous administration. The new government continues to live within its means and to err on prudence. The three-year fiscal plan remains balanced. The plan projects small surpluses of \$246 million in FY17/18, \$228 million in FY18/19 and \$257 million in FY19/20. These are little changed from the surpluses of \$295 million in FY17/18, \$244 million in FY18/19 and \$223 million in FY19/20 projected in the February 2017 budget. The update maintains several prudence measures, including a \$300 million forecast allowance (rising to \$350 million in FY19/20) and conservative economic growth assumptions (still slightly below private sector forecasts).

It's just that the means have increased

The good news for the new government is that British Columbia's strong economy is increasing the means to pursue a spending agenda. The forecast for real GDP growth in 2017 has been revised upwardly from 2.1% in the February budget to 2.9%. Importantly, last year's larger-than-expected budget surplus of \$2.7 billion (compared to \$1.5 billion projected at Budget 2016) set both a higher revenue base and lower expenditure base for the updated fiscal plan than previously assumed. These factors translated into a \$1.5 billion upward revision to revenues in the current fiscal year before the new government even sat down to work on this budget update.

More spending on priority items

With this fiscal room at hand, BC Finance Minister Carole James yesterday announced a series of spending initiatives that totaled \$660 million in FY17/18—rising to \$900 million in FY19/20. Chief among them were the elimination of bridge tolls (\$224 million in FY17/18), increasing funding for education (\$177 million), boosting social assistance rates (\$104 million), more money to address the fentanyl crisis (\$67 million) and increasing investment in housing (\$14 million). These initiatives were on top of previously announced \$669 million to support wildfire emergency response this year.

Taxes are rising for some, cut for others

In terms of new revenue initiatives, Minister James announced a mix of tax increases and cuts that initially brings in little net new revenue this year (\$50 million). The net increase grows materially over time, however, to \$480 million by FY19/20. The new government is moving forward with recalibrating the province's tax structure. It is reinstating a higher personal income tax rate (16.8%) for individuals with taxable income exceeding \$150,000 and raising the general corporate income tax rate from 11% to 12%. It is also increasing the carbon tax by \$5 per tonne to \$35 on April 1, 2018. On the other hand, the government is lowering the small business tax rate from 2.5% to 2% and upholding the previous government's pledge to cut Medical Services Plan premiums by 50%. Minister James indicated that her government is still committed to eliminate these premiums completely, although a decision in this respect has been delayed to a future budget.

The province's capital plan gets a further boost

The February 2017 budget substantially boosted the province's three-year taxpayer-supported capital investment plan to a total of \$13.7 billion. In this update, the new NDP government ramps up projected investment by a further \$930 million to \$14.6 billion. This includes a record \$5.0 billion this fiscal year. The BC Transportation Financing Authority (up \$346 million), health (up \$214 million), education (up \$266 million) and housing (up \$119 million) are getting the lion's share of the \$1.3 billion increase relative to FY16/17. The three-year capital investment plan for self-supported entities (commercial crown corporations) is revised downwardly by \$2.3 billion relative to the February budget to \$8.5 billion. The revision reflects the cancellation of the George Massey Tunnel by the Transportation Investment Corporation. BC Hydro's \$8.8 billion Site C clean energy project is still a go.

Provincial debt rises a little but is still under control

The updated taxpayer-supported debt profile tracks slightly higher than in February's budget but remains well under control. The slight deterioration is due in part to a one-time \$3.5 billion reclassification from self-supported debt to taxpayer-support debt related to the government's decision to cancel tolls on the Port Mann bridge. It also partly reflects stronger expected capital investment throughout the fiscal plan. Taxpayer-supported debt is now projected to increase from \$41.5 billion (15.8% of GDP) at the end of FY16/17 to \$44.5 billion (16.2%) in FY17/18 and \$48.6 billion (16.3%) by FY19/20. The updated terminal point is \$1.4 billion (0.2 percentage points) higher than it was in the February budget—not enough to alter the province's healthy debt position in a meaningful way. The profile for self-supported debt, on the other hand, was lowered significantly in light of Port Mann bridge debt reclassification and cancellation of the George Massey Tunnel replacement project (\$2.4 billion). Total provincial debt is now forecasted to rise from \$65.9 billion at the end of FY16/17 to \$72.8 billion by FY19/20.

Borrowing requirements jump this year

The BC government anticipates to borrow \$3.5 billion in FY17/18, \$2.9 billion of which remains to be done. This year's borrowing would be a sizable increase of \$1.5 billion over FY16/17. The government expects borrowing requirements to climb higher still to \$6.9 billion in FY18/19 before easing to \$5.2 billion in FY19/20.

More to come in 2018?

The measures announced in this budget update should be seen as the NDP government's first steps toward putting their stamp on the province after 16 years of Liberal administrations. A number of key (and expensive) electoral commitments—including \$10 a day daycare and complete elimination of Medical Services Plan premiums—have not been fulfilled this time around but remain on the government's to-do list. The upcoming 2018 budget no doubt tell us more about the next steps. For now, we're encouraged to see that the first steps stayed within the province's means. Hopefully this will remain a guiding principle.

British Columbia's fiscal plan

\$ billions	Actual	Budget	Update	Plan	Plan
	<u>16/17</u>	<u>17/18</u>	<u>17/18</u>	<u>18/19</u>	<u>19/20</u>
Total revenues	51.5	50.8	52.4	52.6	53.7
Total expenses	48.7	50.2	51.9	52.0	53.1
Program spending	46.1	47.5	49.2	49.2	50.2
Interest on public debt	2.6	2.7	2.7	2.8	2.9
Surplus (before forecast allowance)	2.737	0.645	0.546	0.528	0.607
Forecast allowance		-0.350	-0.300	-0.300	-0.350
Surplus	2.737	0.295	0.246	0.228	0.257

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