Rating Report

Province of British Columbia

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DBRS

Insight beyond the rating.

Ratings

Debt	Rating	Rating Action	Trend
Issuer Rating	AA (high)	Confirmed	Stable
Long-Term Debt*	AA (high)	Confirmed	Stable
Renminbi Bonds	AA (high)	Confirmed	Stable
Short-Term Debt*	R-1 (high)	Confirmed	Stable

* Includes the Long-Term and Short-Term Obligations of British Columbia Hydro and Power Authority based on its status as a Crown agent.

Rating Update

DBRS Limited (DBRS) confirmed the Issuer Rating, Long-Term Debt rating and Renminbi Bonds rating of the Province of British Columbia (B.C. or the Province) at AA (high) as well as the Short-Term Debt rating at R-1 (high). All trends are Stable. The ratings remain well supported by the Province's diverse and growing economy, positive budget outlook, ample fiscal capacity and low debt burden.

In July 2017, the New Democratic Party (NDP) assumed power after 16 years in opposition. This change in government has led to a significant shift in tax and fiscal policy, with a considerable focus on improving affordability and enhancing public services. The new government has an ambitious policy agenda, and the 2018 budget suggests that total expense may rise by nearly 20.0% over the course of the government's four-year mandate. The new government has sought to temper concerns about the pace of spending growth by emphasizing its commitment to balanced budgets, conservative budgeting practices and ongoing focus on debt affordability. Nevertheless, with a short time in government there remains a degree of uncertainty as to the pace of program growth, tolerance for deficit spending through the business cycle, upcoming labour negotiations and management of the Province's large government business enterprises.

The Province's 2018 budget continues to align with the core policy priorities outlined by the NDP since taking power. The budget provides for moderate growth in spending (+5.2% on a DBRS-adjusted basis) with a focus on affordable housing and child care. The fiscal plan continues to target modest surpluses over the three-year forecast horizon and incorporates considerable contingencies. On a DBRS-adjusted basis, the deficit is estimated to be $2.6 billion, or 0.9% of gross domestic product (GDP), in 2018–19.

The Province's economy has expanded quickly in recent years. Growth has been relatively broad based, with gains in consumption, investment and trade supported by the improving global economy, low interest rates and moderate population growth. With annual growth in the range of 3.0% to 4.0% over the last four years, the Province is now projecting growth will slow to 2.3% in 2018 and 2.0% in 2019, which is somewhat weaker than the private-sector consensus tracked by DBRS. This should keep the Province's DBRS-adjusted debt burden stable at around 17.5% through the medium term.

Continued on P.2

Financial Information

	For the year ended March 31				
	2019B	**2018P**	**2017**	**2016**	**2015**
Debt/GDP	17.3%	17.4%	17.5%	18.8%	19.2%
Surplus (deficit)/GDP	(0.9%)	(0.6%)	0.6%	(0.5%)	(0.2%)
Federal transfers/total revenue	16.9%	16.7%	16.3%	16.7%	16.4%
Interest costs/total revenue	3.5%	3.3%	3.2%	4.1%	3.7%
Real GDP growth	2.0%	2.3%	3.4%	3.5%	3.5%

Notes: Debt is defined as net taxpayer supported + municipal debt + unfunded pension liabilities. B = budget. P = projected. GDP on a calendar-year basis , 2017 and subsequent years are Ministry of Finance forecasts.

Issuer Description

B.C. is Canada's westernmost province, located along the Pacific Ocean. The Province has a population of 4.8 million and is the fourth-largest provincial economy in the country by GDP. The Province has a diverse and stable economy, with real GDP of about of $250.0 billion.

Rating Update (CONTINUED)

No rating action is anticipated in the near term. A positive rating action requires the Province to maintain a sustainable budgetary position and have its DBRS-adjusted debt-to-GDP ratio fall to, and remain below, 15.0%. A negative rating action could arise from a sustained deterioration in operating results and marked increased in the debt-to-GDP ratio.

Rating Considerations

Strengths

1. Stable, growing economy
B.C. has a diverse and growing economy. Among provinces, economic growth in B.C. has tended to be among the strongest in recent years, ranging between 2.5% and 3.7%. The provincial economy benefits from its advantageous location along the West Coast, a skilled workforce, consistent population growth and a diverse industrial mix.

2. Disciplined fiscal policy
While many governments have stated their commitment to balanced budgets, low taxes and prudent expense management, B.C. has consistently demonstrated its commitment to these principles over the past decade. The Province has maintained a sustainable budget position for a number of years, and the Province's balance sheet has largely recovered to its pre-recession state. While there is a degree of policy uncertainty with the change in government, the new government has committed to maintain budget surpluses, use conservative budgetary practices and continue focusing on debt affordability.

3. Low debt burden
B.C. has one of the lowest debt burdens among provinces and only modest unfunded pension liabilities. The budget suggests that the DBRS-adjusted debt-to-GDP ratio will stabilize around its current level over the medium term (17.5% of GDP). The low debt burden results in relatively low interest costs and greater flexibility to absorb the impact of rising interest rates. The Province's debt profile is tilted toward the longer end, with a weighted-average term-to-maturity of 14.1 years (up from 13.9 years as at March 31, 2017).

4. Fiscal capacity
The Province has a relatively lower tax burden when compared with most other provinces, which provides the government with flexibility to raise revenue to address budget pressures should they emerge.

Challenges

1. Some policy uncertainty
The change in government gave rise to a degree of policy uncertainty — fiscal, economic and social. The new government has outlined an extensive policy agenda but remains committed to balanced budgets and debt affordability as policy anchors. The government has only been in power for eight months during a strong economic expansion after 16 years in opposition. With competing priorities, it will be some time before the government demonstrates a consistent record of prudent budget management.

2. High level of household indebtedness
The rapid increase in home prices and historically low interest rates have resulted in elevated household indebtedness, which could amplify the severity of an external shock to the provincial economy and, by extension, the Province's fiscal plan.

3. Affordability challenges
Greater Vancouver and, to a lesser extent, Greater Victoria are among the least-affordable regions in Canada, posing challenges for residents and businesses. The lack of affordability has prompted a policy response by government. While initial measures have been modest relative to the extent of the challenge, the new government would likely undertake further measures should they prove necessary. New policy measures could put pressure on the Province's fiscal plan or could result in unintended consequences in the marketplace.

2018–19 Budget

Exhibit 1: DBRS-Adjusted Surplus (Deficit)-to-GDP

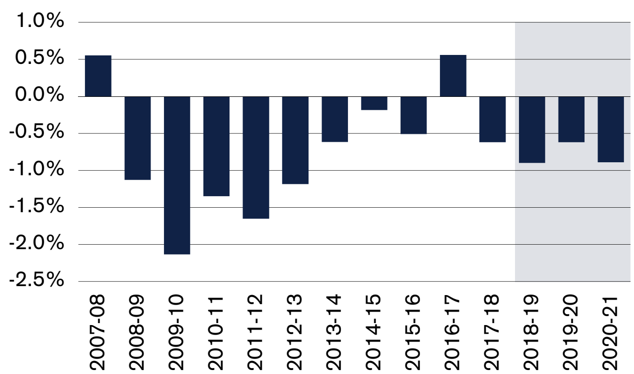
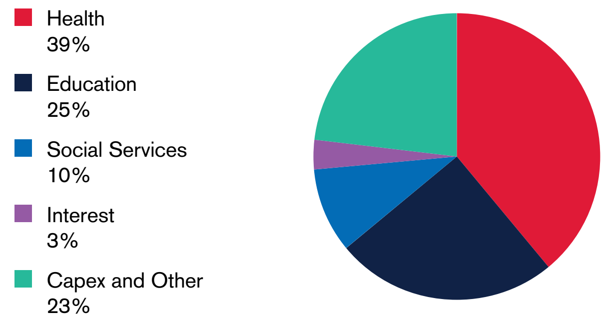


Exhibit 2: DBRS-Adjusted Spending



The 2018 budget was consistent with the expectations set out previously by the government, with major program and policy announcements focused on the government's core policy priorities:

- Making life more affordable.
- Improving public services.
- Ensuring all British Columbians share in the economic prosperity of an innovative economy.

While the government has an ambitious agenda for the coming years, it continues to reiterate its commitment to debt affordability, prudent budgeting and positive operating results. The budget projects a surplus of $219 million in 2018–19, which equates to a DBRS-adjusted deficit of $2.6 billion, or 0.9% of GDP. DBRS makes the following adjustments to B.C.'s reported results/budget projections to improve comparability between provinces and over time:

- The addition of capital investment to and removal of capital amortization from program expense.
- The exclusion of the net change in regulatory accounts from the net income of BC Hydro.
- The exclusion of the forecast allowance and non-recurring items.

B.C. continues to use conservative budgeting practices. These measures are intended to address unforeseen spending pressures, revenue volatility and statutory spending (e.g., response to disasters, litigation, etc.). In the past, the adoption of prudence in its budget estimates has enabled the Province to outperform budget projections in most years. For 2018–19, explicit measures of budgetary conservatism include:

- The use of a below-consensus economic forecast-to-project revenue (real GDP growth is 0.2 percentage points lower than consensus).
- An explicit forecast allowance to reduce the budgeted surplus ($350 million).
- An explicit expense contingency to offset unexpected pressures and fund priority initiatives ($550 million).
- A relatively low natural gas price for the natural resource revenue forecast (20th percentile of the private-sector survey).

The Province has projected modest revenue growth for 2018–19 (+3.6% on a DBRS-adjusted basis), following 4.8% average annual growth over the previous three years. Revenue growth in 2018–19 is projected to be relatively broad based, with improvements in tax revenue (+4.8%; includes Medical Services Plan (MSP) premiums for comparability), government business enterprises (+6.3%) and federal transfers (+4.5%). Gains in these categories will be offset by some weakness in resource revenue (-6.7%), which reflects an expected decline in bonus bids and mining revenues as well as an expected decline in lumber prices.

The new government announced a series of major tax policy changes in its first two budgets. These changes have altered the distribution of the tax burden among taxpayers but has not significantly changed the overall tax burden on the economy. On balance, the changes reduced total tax revenue in 2017–18, left total tax revenue roughly unchanged in 2018–19 and will result in modestly higher revenue in 2019–20. The major tax policy announcements contained in the 2018 budget are as follows:

- Introduction of a new tax on properties held by in certain urban areas that are not occupied as a principal residence or rented out long term (Speculation Tax) and increases in property and property transfer taxes on properties valued at more than $3.0 million. The foreign buyers' tax was also extended to other regions in the Province.
- Replacement of the Medical Service Plan (MSP) premiums with a new payroll tax (Employer Health Tax) which will come into effect on January 1, 2019. The rate structure will be graduated with a maximum rate of 1.95%. The new tax rate is the same as the payroll tax rate levied by the Province of Ontario, also called the Employer Health Tax.

2018–19 Budget (CONTINUED)

While the overall tax burden has not changed significantly, the changes appear to have modestly increased the marginal effective tax rate on new business investment.

Total DBRS-adjusted expenditures are projected to rise by $2.7 billion (+5.2%) in 2018–19, which follows projected expenditure growth of $4.1 billion (+8.3%) in the prior year. Spending growth is broad based, with most ministries set to see their budget allocations increase. All core areas of government will see moderate to strong increases: health (+4.0%), education (+4.6%) and social services (+12.6%). Spending growth is being partially offset by anticipated declines in the justice- and resource-related ministries, whose budgets increased in 2017–18 because of the wildfires.

The central focus of the budget was affordable housing and child care, which aligns with the elected government's core policy priorities and begins to address some of the major concerns commonly raised by British Columbians and business groups.

- **Housing Affordability ($1.6 Billion over Three Years):** The budget contained 30 measures that, collectively, seek to stabilize the housing market, improve affordability for lower-income households and address fraud/tax evasion. The policy objective is to return the housing market to trend, as opposed to reducing prices or improving home ownership rates. The measures are intended to provide targeted support to lower-income households, support the development of purpose-built rental/affordable housing and improve the supply of privately owned rental housing policies and initiatives intended to stabilize the B.C. housing market (includes tax and non-tax measures). Further measures are likely forthcoming should these prove inadequate.
- **Child Care ($1.0 Billion over Three Years):** The Province is introducing a suite of initiatives to improve the availability, quality and cost of child care. Initiatives include the introduction of a new affordable child-care benefit and child-care fee reduction program; funding for 22,000 new child-care spaces; and increased funding for early childhood education. The budget messaging suggests that further announcements will be forthcoming as the Province works toward universal child care.

The other major policy-related spending announcements contained in the budget include increased funding for team-based primary health care, increased spending on seniors' care and early-learning, teacher-hiring and transportation subsides.

Capital investment is set to rise sharply in 2018–19 (+23.3%) and to remain elevated over the medium term. In 2018–19, transportation infrastructure and housing account for the bulk of the year-over-year increase. This is a record level of capital investment for the Province. In recent years, actual capital investment has been 5.0% to 15.0% lower than planned.

Outlook

Having spent 16 years in opposition, the new government has quickly shifted policy focus, ramped up spending in core program areas and introduced significant tax policy changes.

The multi-year plan envisions spending increases as the new government rolls out its social policy agenda (e.g., affordable housing, universal child care, poverty reduction, enhancements to early learning, postsecondary education and social assistance benefits). The new government has acknowledged that its policy agenda is significant in scope and has sought to temper concerns about the pace of spending growth by emphasizing its commitment to balanced budgets, conservative budgeting practices and debt affordability. Similar to previous budgets, the Province has outlined a thin track of budget surpluses over the next three years and has incorporated $2.6 billion in unallocated spending in the outer years to accommodate future spending pressures, government priorities and a new wage mandate.

Having only assumed power in July 2017, the NDP government has yet to develop a track record of responsible financial management. While early messaging suggests positive operating results and a stable debt-to-GDP ratio, there remains some uncertainty as to the pace and sustainability of spending growth, the new government's tolerance for deficit spending through the business cycle, the outcome of upcoming collective bargaining and the management of the largest government business enterprises (i.e., Insurance Corporation of British Columbia (ICBC) and BC Hydro).

Public-Sector Bargaining

The Province has identified public-sector bargaining as one of the medium-term risks to the fiscal plan. Most of the Province's collective agreements expire at the end of the current fiscal year or early in the next fiscal year. B.C. has among the strongest models for public-sector bargaining that centralizes and coordinates bargaining across the public sector (182 collective agreements), thereby enabling a degree of consistency, limiting opportunities for leapfrogging and diminishing political interference. An NDP government in the 1990s introduced the model to create space between the elected government and the unions. At this time, there is no indication the model is likely to change.

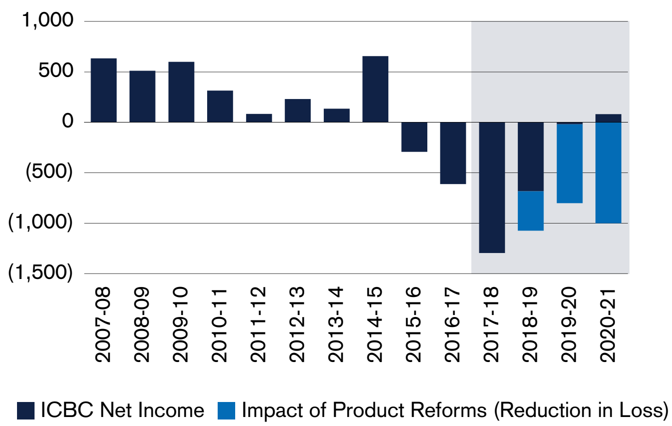
The elected government is responsible for setting and approving bargaining mandates. The Province is now in the process of developing the next bargaining mandate, and DBRS understands that the elected government and employers are seeking to manage expectations for compensation increases. Nevertheless, DBRS expects the upcoming mandate to be as generous, or possibly more generous, than the previous mandate in light of the strength of the underlying economy and tightening labour market. With total public-sector compensation expected to be about $30.0 billion in 2019–20, a one-percentage-point increase in compensation accounts for about $300 million in added expense.

2018–19 Budget (CONTINUED)

The last public-sector bargaining mandate was the Economic Stability Mandate (2014), which allowed for modest compensation growth (5.5% over five years) and the opportunity to share in the Province's economic growth through an economic stability dividend (ESD). To the extent that real GDP growth exceeded the government's independent Economic Forecast Council forecast, employees have been receiving wage increments equivalent to 50% of the positive difference between actual and projected real GDP growth for a given year. From 2015/16 – 2017/18, ESD increases totalled 1.2% over the three years. Based on the most recent estimate for 2017 real GDP growth, labour groups could receive a further wage increase in 2018/19 of 0.55% on account of the final 2017 ESD.

Insurance Corporation of British Columbia

Exhibit 3: ICBC Net Income ($ Millions)



Source: Province of British Columbia.

ICBC is a wholly owned Crown corporation that provides compulsory vehicle insurance (basic) and optional additional vehicle insurance (competitive market) in the Province.

ICBC's operating results have deteriorated significantly in recent years, with the Crown corporation now expecting to record of a loss of $1.3 billion in 2017–18. The causes of the deterioration include:

- An increasing number of collisions.
- An increasing number of injury claims per collision.
- Increasing costs associated with settling claims for minor injuries, in part because of the absence of claim limits for pain and suffering and the use of the courts for dispute resolution.
- Basic compulsory rates not rising enough to meet increasing claim costs. The Province introduced a rate smoothing mechanism in 2013 that limited annual basic rate changes to +/- 1.5 percentage points from the prior year's approved rate change. The gap between basic insurance claims and premiums is now estimated to be about over $400 million.
- Weaker investment earnings from lower interest rates.

The Province's 2017 budget update in September 2017 projected that ICBC's loss for 2017–18 would be $225 million. In early January 2018, ICBC revised the estimated loss to $1.3 billion. The unexpected deterioration occurred because of a sudden surge in the number and size of claims, which is thought to have been prompted by the increasing public expectation for ICBC reforms that began last summer (i.e., claimants seeking to lodge their disputes before reforms are implemented).

ICBC is fully backstopped by the Province. In the absence of reforms, losses would reasonably have been expected to put pressure on the Province's finances and eventually require capital injections or other forms of support to offset a weakening capital ratio. The Province announced major changes that will be phased in over the next two years to address the weak financial outlook, keep rates affordable, reduce benefits and provide better care for those injured in collisions. The major elements to improve financial results include:

- Limiting awards for pain and suffering in minor injury claims to $5,500. The average claim was $30,038 in 2016.
- Using the B.C. Civil Resolution Tribunal to review minor injury claims disputes, as opposed to the court system.
- Addressing disparities in rates to better align costs with risk and make basic insurance rates fairer.
- Introducing new measures to reduce collisions.
- Improving ICBC's cost effectiveness.

Product reforms — to be phased in over the next two years — are expected to improve operating results by $1.0 billion once fully implemented. As such, the forecast projects that losses will remain wide in the near term but decline as old claims are settled and savings from the product reforms take hold. The Province has indicated that these estimates include an element of conservatism given the evolution of results in recent years. They do not include any possible savings that may result from the operational review currently underway, nor do they incorporate savings that may result from behavioural changes stemming from road-safety measures.

The British Columbia Utilities Commission (BCUC) is ICBC's principal regulator and responsible for approving rate increases. Past intervention by governments has limited the BCUC's regulatory flexibility. DBRS understands that the current government may make changes to improve regulatory oversight and authority, though the rate-smoothing mechanism appears unlikely to change in the near term. Ultimately, a move to increase regulatory oversight and independence that sustainably improves operating results would be viewed positively for the Province's credit profile.

2018–19 Budget (CONTINUED)

British Columbia Hydro and Power Authority

BC Hydro, the Province's wholly owned and controlled electric utility, has operated under the direction provided in the Province's 2013 ten-year rates plan for the utility. The Province has sought to maintain low and competitive electricity rates and has set BC Hydro's net income targets through directives from 2017–18 onward ($698 in 2017–18 and $712 in 2018–19 and onward).

During the 2017 election, the NDP made a number of commitments that could have a significant and adverse impact on BC Hydro's financial results and, by extension, the Province's financial results. These commitments include a review to determine whether it was in British Columbians' best interests to continue with the Site C Clean Energy Project, a comprehensive review of BC Hydro and a rate freeze. The policy direction is now clearer, and the risks posed to the Province's credit profile have diminished.

- **Site C Clean Energy Project:** Construction of a 1,100-megawatt hydroelectric generating station. The Province decided to continue with the project in December 2017, and the budget was revised higher to $10.7 billion (from $8.775 billion). The budget includes an $800 million contingency and $700 million in reserves. The 2024 target in-service date remains unchanged, and the Province has increased project oversight. Major risks to the project's budget/in-service date remain geotechnical challenges, reliance on multiple contractors and their phasing of the project, and litigation. First Nations are challenging the construction project on the basis that it infringes on their treaty rights.
- **Rate Freeze Commitment:** BC Hydro applied to the BCUC for a one-year rate freeze in light of the government's commitment to freeze rates while it conducted its review of the utility (part of its goal of improving affordability for households and businesses). However, following comments by the Premier in the media casting doubt on the appropriateness of a blanket rate freeze, the BCUC directed BC Hydro to raise rates by the originally requested 3.0% for the 2018–19 fiscal year. The government's response to the rate decisions suggests that the government is now inclined to adopt a more targeted approach to addressing electricity costs for lower-income households and interfering less in the regulatory process. DBRS expects that rate relief for lower-income households is likely to be funded through other ratepayers, as opposed to the fiscal plan (taxpayers), and that the government will make an announcement during the spring legislative session.
- **Strategic Review:** There is now clarity regarding the intent of the strategic review of BC Hydro. While past reviews have focused on efficiency gains, this review has a somewhat different focus. The review will consider (1) the balance of power and responsibilities between the government and the BCUC, (2) the strategic outlook and transformational changes and (3) longer-term affordability. DBRS understands from discussions with Cabinet Ministers and other senior officials that the new government intends to increase the independence of the BCUC and rely less on government directives. DBRS views this as a positive development, as it reduces the risk that political interference in BC Hydro could ultimately harm the credit profile of the Province.

At this time, there have been no changes to the utility's ten-year rates plan, though DBRS expects changes could be forthcoming as a result of the various initiatives. The Province remains committed to improving the capital structure of the utility (target debt-to-equity of 60/40; currently at around 80/20), which supports DBRS's view that BC Hydro's debt is indeed self-supporting and reduces the longer-term risk posed by the utility on the government's fiscal plan and balance sheet.

2017–18 Preliminary Results

The Province has projected a surplus of $151.0 million for the year ended March 31, 2018, which is modestly lower than what was expected in the fall budget update ($246 million). On a DBRS-adjusted basis, this equates to a deficit of $1.7 billion, which is well ahead of expectations for a $2.5 billion shortfall. The better result was primarily because of lower-than-planned capital spending, the impacts of improved economic growth during the year and drawing down a portion of the budgeted forecast allowance.

Despite a robust economy, DBRS-adjusted revenue growth was modest at $861 million (+1.7%). Revenue growth was weaker because of unusual volatility in underlying personal income tax (-8.4%) revenue resulting from federal rate changes in 2016, a rapid deterioration in ICBC's net income during the year and other policy changes (e.g., reduction in MSP premiums). Overall, own-source revenue was projected to be 1.1% higher, while federal transfers were projected to be 4.7% higher owing to ongoing growth in health and social transfers and support for the 2017 wildfires.

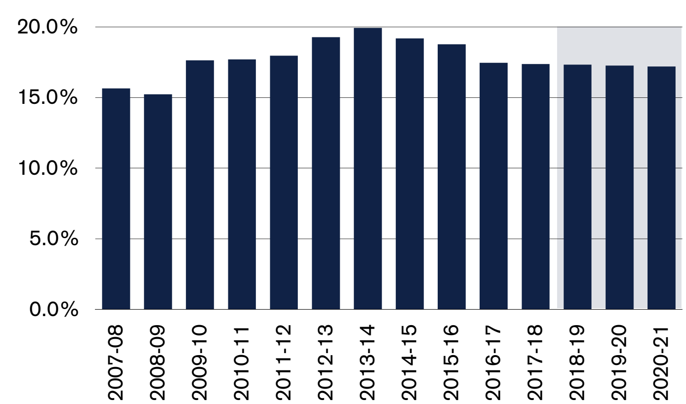
DBRS-adjusted expenditures were significantly higher (+8.3%) during the year, which reflects the surge in pre- and post-election spending and the costs associated with wildfire response (approximately $875 million).

Debt Profile

B.C. has the lowest debt burden among provinces. In 2017–18, DBRS-adjusted debt rose by $2.5 billion to $48.6 billion. The increase was largely because the Province eliminated tolls on the Port Mann Bridge, which resulted in $3.5 billion in self-supported debt being reclassified as taxpayer-supported debt (equivalent to 1.3 percentage points of GDP). As a share of GDP, debt was stable at 17.4%.

The debt profile is largely unchanged, with a prudent maturity profile, no unhedged foreign currency exposure and a limited amount of floating-rate debt (20% of the debt stock). The Province has an internal oversight committee, which advises the Ministry of Finance on the borrowing program and provides oversight.

Exhibit 4: DBRS-Adjusted Debt-to-GDP



Sources: Province of British Columbia and DBRS calculations.

The Province issues debt in both domestic and international markets, often looking for opportunities to reduce its overall borrowing costs. It has established borrowing programs in the United States, Europe and Australia. The Province does not have an explicit policy or guideline dictating domestic/foreign issuance, but the Province will generally go offshore if the all-in cost is lower than what is available in the domestic market. As at February 20, 2018, about $10.2 billion (17%) of gross market debt outstanding was sourced outside of the domestic market. The foreign currency exposure is fully hedged back to Canadian dollars.

As at February 20, 2018, the Province was party to derivatives contracts with notional principal amounts totalling $15.6 billion, consisting largely of foreign currency and interest rate swaps. The Province has an internal policy that limits its counterparties to high-quality financial institutions with higher standards for longer-dated swaps.

Like other provinces, B.C. has sought to extend the term of its debt profile to lock in lower interest rates. The average term to maturity is projected to be 14.1 years as at March 31, 2018. The maturity profile is relatively smooth over the next decade, with the Province generally targeting to have no more than $5.0 billion maturing in any given year. The Province has reduced the size of its short-term promissory note program in recent years and continues to focus its domestic issuance on larger benchmark issues.

B.C. maintains considerable liquidity relative to the size of its short-term program (typically $3.0 billion to $4.0 billion) and its long-term borrowing requirement. In the narrowest sense, the Province has cash balances ($3.1 billion, on average, in 2017–18) and special-purpose investments ($1.0 billion) that can be readily accessed in the event of a broad market disruption. The Province could further access liquidity in the broader public-sector entities it controls or draw on a $400 million credit facility.

The Province has limited unfunded pension liabilities. As at March 31, 2018, these are projected to be $187 million (0.1% of

Debt Profile (CONTINUED)

GDP). Unfunded pension liabilities are expected to remain low. The Province's major pension plans are defined-benefit/defined-contribution hybrid plans. They provide a basic guarantee, but indexation is on a defined-contribution basis. In addition, the plans have joint trusteeship, with employers and employees equally sharing risk, which results in more proactive management.

Outlook

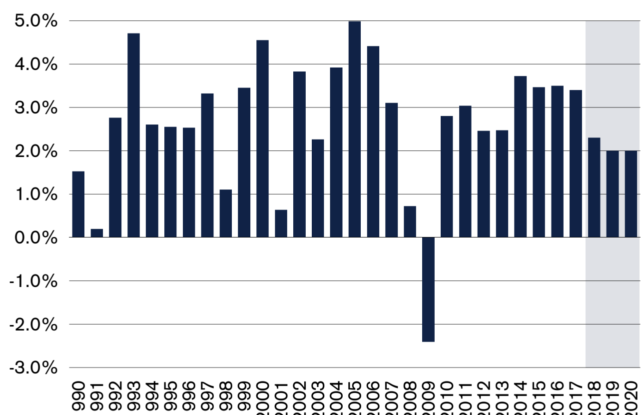
The Province continues to stress its focus on prudent and responsible fiscal policy and, ultimately, debt affordability. In considering the affordability of its debt, the Province typically looks at debt as a share of revenue and GDP. Debt-to-revenue is set to rise modestly, while debt-to-GDP is expected to remain stable over the medium term at around 17.5%.

The 2018–19 borrowing program totals $7.7 billion, which is a significant increase over the borrowing programs of recent years. The larger plan reflects the expanded capital programs being undertaken by the Province and by BC Hydro. The Province expects to maintain duration at seven-plus years, maintain liquid benchmarks (ten-year and 30-year bonds) and opportunistically diversify funding sources. The Province does not have a specific target for domestic/U.S./international issuance.

Over the medium term, debt will continue to rise with the expanding capital program, though the DBRS-adjusted debt-to-GDP ratio is likely to remain stable at around 17.5% of GDP if the Province continues to maintain a balanced operating budget. The capital plan remains silent on the George Massey Tunnel Replacement (GMTR) Project, for which procurement was cancelled last fall. With the elimination of road tolls, the GMTR Project is likely to require taxpayer-supported debt. There is no clarity on the size, scope or timing of the project. However, the estimate for the previous project was $3.5 billion (equivalent to about 1.2% of GDP).

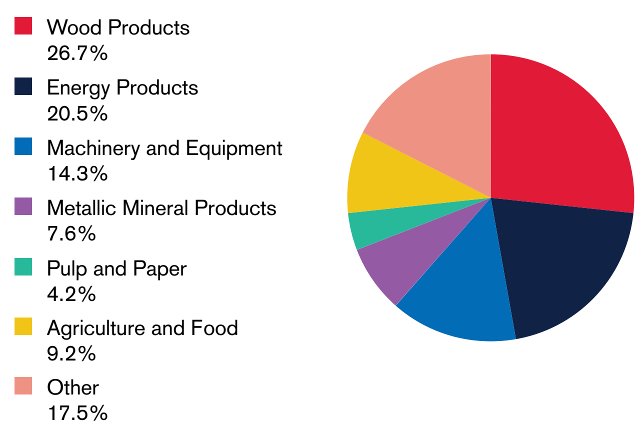
Economy

Exhibit 5: Economic Growth (Real GDP Growth (%))



Sources: Statistics Canada, Haver Analytics and Province of British Columbia.

Exhibit 6: Exports to the United States (Goods Exports (2017))



Source: Statistics Canada.

B.C. is one of Canada's larger provinces with a population of 4.8 million and economic output of about $250.0 billion annually. The Province has experienced consistent population and economic growth in recent years, which reflects, in part, the diversity of the provincial economy and the desirability of the region as a place to live. The primary sector (fishing, farming and resource extraction) accounts for a relatively small share of provincial output (7.7%), and the goods sector, more broadly, only accounts for about 25.0% of output.

The Province has only experienced one contraction (2009) over the last 20 years, and in recent years, economic growth has typically ranged between 2.5% and 3.7% annually, which is also consistently above the Canadian growth rate.

The Province continues to experience moderate population growth with annual increases in the range of 1.0% to 1.3%. The population's age profile resembles that of Ontario (rated AA (low) with a Stable trend by DBRS) and the Province of Québec (rated A (high) with a Stable trend by DBRS). The population is somewhat older (median age of 42.1 years), and while births continue to outpace deaths, international and interprovincial migration have been the major population growth drivers in recent years. Interprovincial migration surged during 2014–16 with the downturn in the Province of Alberta's (Alberta; rated AA with a Negative trend by DBRS) economy but has since moderated. Nevertheless, the Province expects moderate population growth to persist through the medium and longer term.

Economy (CONTINUED)

The economy continued to expand at a relatively strong pace in 2017 (+3.4%). In recent years, growth has been broad based, with gains in consumption, investment and trade supported by an improving global economy and the persistence of accommodative monetary policy. The Province and private-sector economists expect growth to moderate in the coming years, with growth returning to a more sustainable pace. Low interest rates have supported strong growth in retail sales, motor vehicle sales and housing consumption, which should moderate with the rising interest rates.

The improving economic outlook has translated into significant gains in the labour market. In 2017, employment expanded at its fastest pace in two decades, with gains primarily in full-time and private-sector positions. The unemployment rate fell to 5.1% — its lowest level since 2008 and likely below the natural rate of unemployment. The Province is experiencing some labour shortages in select industries (i.e., construction, tourism, hospitality, transportation and technology), though wide-spread wage pressures have yet to emerge. As the pace of economic growth moderates, the Province expects employment growth to slow and for the unemployment rate to rise modestly.

B.C. recently announced that it would raise the minimum wage to $15.20 (+33.9%). Consistent with the recommendations of the Fair Wages Commission, the increase will be phased in over a four-year period, with larger annual increases in 2018 and 2019. The increases may contribute to modestly higher youth unemployment and accelerate the trend toward greater automation, but they are not expected to have a significant impact on the overall labour force or economy.

The Province expects the housing market to begin to stabilize. In 2017, housing starts rose (+4.4%) to their highest level in six decades, though price growth slowed (+2.7%) and sales declined modestly from a record high in the prior year. The Province's economic forecast, does not incorporate the impact of the housing market measures announced in the budget but does expect a decline in housing starts (-26.8%) toward historical trend, a modest decline in the value of residential sales (-3.1%) and moderate price growth. The expected moderation in activity is partly the result of Office of the Superintendent of Financial Institutions changes and rising interest rates, which should be reinforced by the housing market measures introduced in the 2018 budget.

The outlook for trade also poses some risk to the provincial economy. While trade is important for B.C.'s economy, the Province is somewhat less exposed than other Provinces. Overall, imports and exports account for a relatively smaller portion of economic activity, and among provinces, B.C. has a lower direct exposure to the U.S. market. The United States accounts for about half of the Province's goods exports. In contrast, the United States accounts for about 80% of Ontario's exports and 90% of Alberta's exports.

B.C.'s largest goods exports to the United States are wood products (26.7%), energy products (20.5%), machinery and equipment (14.3%) and metallic mineral products (7.6%). The largest export states are Washington and California.

Softwood lumber accounts for much of B.C.'s wood product exports, and the Unites States accounts for about two-thirds of softwood exports. While softwood lumber continues to account for a large share of the Province's exports, its relative importance in the provincial economy has diminished over the last two decades as a result of growth in other industries, particularly services. The forestry industry accounts for about 3.0% of economic activity in the Province and about 60,000 jobs. The United States has imposed duties ranging between 20.0% and 24.0% on B.C. producers. However, with strong U.S. demand for lumber, transportation-related issues and the impacts of the wildfires and beetles, prices have remained elevated, thereby limiting the impact of the duties on producers/communities.

The outlook for resource development remains muted in the Province. The sharp declines in North American and Asian natural gas prices have led many proponents of major liquefied natural gas (LNG) projects to defer, delay or cancel projects. DBRS does not expect significant development of LNG facilities to occur over the next five years. Nevertheless, the Province remains supportive of LNG development in the Province, despite its stated opposition to the Kinder Morgan, Inc. (rated BBB (low) with a Stable trend by DBRS) Trans Mountain Pipeline expansion and the development of bitumen export capacity. On March 22, 2018, the Province announced changes to the LNG development framework ahead of a meeting with the LNG Canada joint venture partner. The changes to the framework reduced the tax burden on development. LNG Canada is set to make a decision toward the end of 2018.

Outlook

The Province and private-sector economists are projecting for economic growth to moderate in the coming years, with growth expected to slow to 2.3% in 2018 before steadying around 2.0% over the medium term. Risks to the economic outlook include U.S. trade and fiscal policy, monetary policy and possible economic disruption in Asia or Europe.

Economic Statistics	2019	2018	2017	2016	2015	2014	2013
Nominal GDP ($ millions)	303,294	291,672	279,370	263,706	251,744	242,044	228,973
Nominal GDP growth	4.0%	4.4%	5.9%	4.8%	4.0%	5.7%	3.4%
Real GDP growth	2.0%	2.3%	3.4%	3.5%	3.5%	3.7%	2.5%
Population (thousands)	4,925	4,869	4,817	4,758	4,695	4,646	4,590
Population growth	1.2%	1.1%	1.3%	1.3%	1.0%	1.2%	1.0%
Employment (thousands)	2,529	2,501	2,467	2,380	2,306	2,278	2,266
Unemployment rate	5.6%	5.4%	5.1%	6.0%	6.2%	6.1%	6.6%
Housing starts	30,008	31,965	43,664	41,843	31,446	28,356	27,054
Retail sales ($ millions)	91,234	87,910	84,301	76,885	71,614	67,001	63,053
Inflation rate (CPI)	2.0%	2.0%	2.1%	1.8%	1.1%	1.0%	-0.1%
Household income per capita ($)	53,549	52,160	50,661	48,828	47,329	45,246	44,249

Sources: Statistics Canada, CMHC and Ministry of Finance estimates and projections.

Budget Summary	Budget		Budget			
($ millions)	2018–19	2017–18	2017–18	2016–17	2015–16	2014–15
Revenue	52,928	51,100	51,135	50,239	45,845	44,379
Program expenditure	(53,716)	(51,143)	(51,858)	(47,156)	(45,261)	(43,191)
Program Surplus (Deficit)	**(788)**	**(43)**	**(723)**	**3,083**	**584**	**1,188**
Interest costs	(1,836)	(1,684)	(1,764)	(1,605)	(1,865)	(1,638)
DBRS-Adjusted Surplus (Deficit)	**(2,624)**	**(1,727)**	**(2,487)**	**1,478**	**(1,281)**	**(450)**
DBRS adjustments:						
Non-recurring revenue (expenditures)	98	274	298	549	361	130
Capital assets bought less amortized	2,831	1,903	2,672	1,021	1,256	1,250
Adjustment for B.C. Hydro deferrals	264	(199)	63	(311)	475	734
Forecast allowance	(350)	(100)	(300)	-	-	-
Surplus (Deficit), as Reported	**219**	**151**	**246**	**2,737**	**811**	**1,664**
Capital investment	5,174	4,197	4,956	3,659	3,459	3,407
Gross borrowing requirement	7,732	1,969	3,295	3,767	5,110	5,644
Total Tax-Supported Debt	**50,553**	**48,560**	**49,880**	**46,066**	**47,261**	**46,440**

Notes: DBRS reports B.C. Hydro net income before regulatory account transfers for comparability with other provincially owned utilities. Debt is defined as net taxpayer supported + municipal debt + unfunded pension liabilities.

Selected Financial Indicators	Budget		Budget			
(DBRS adjusted)	2018–19	2017–18	2017–18	2016–17	2015–16	2014–15
Debt as share of GDP	17.3%	17.4%	17.9%	17.5%	18.8%	19.2%
Surplus (deficit) as share of GDP	(0.9%)	(0.6%)	(0.9%)	0.6%	(0.5%)	(0.2%)
Surplus (deficit) as share of revenue	(5.0%)	(3.4%)	(4.9%)	2.9%	(2.8%)	(1.0%)
Interest costs as share of revenue	3.5%	3.3%	3.4%	3.2%	4.1%	3.7%
Total tax revenue as share of revenue	57.8%	55.2%	55.1%	53.9%	53.1%	52.0%
Federal transfers as share of revenue	16.9%	16.7%	16.4%	16.3%	16.7%	16.4%
Natural resource revenue as share of revenue	4.6%	5.1%	4.7%	5.4%	5.6%	6.6%
Program expenditure as share of revenue	101.5%	100.1%	101.4%	93.9%	98.7%	97.3%
Health expenditures as share of expenditures	39.0%	39.4%	38.7%	40.4%	40.7%	41.0%
Total revenue growth	3.6%	1.7%	1.8%	9.6%	3.3%	5.5%
Total expenditure growth	5.2%	8.3%	10.0%	3.5%	5.1%	3.1%
Program expenditure growth	5.0%	8.5%	10.0%	4.2%	4.8%	3.0%

Background Political Information

Party in Power:	New Democratic Party	**Legislature Seats:**	41 of 87
Premier:	John Horgan	**Election Required By:**	May 2021

Statement of Operations (DBRS adjusted)

($ millions)	Budget 2018–19	2017–18	Budget 2017–18	2016–17	2015–16	2014–15
Revenue						
Personal income tax	9,836	8,886	9,053	9,704	8,380	8,076
Sales tax	7,428	7,129	7,042	6,606	5,990	5,762
Corporate taxes	4,691	4,741	4,878	3,552	3,307	3,117
Property & property transfer taxes	4,861	4,515	4,259	4,305	3,752	3,219
Payroll tax	463					
Fuel tax	1,003	995	975	969	973	932
Carbon tax	1,488	1,248	1,228	1,220	1,190	1,198
Tobacco tax	822	710	745	737	734	752
Total Tax Revenue	**30,592**	**28,224**	**28,180**	**27,093**	**24,326**	**23,056**
Forests	992	992	890	913	865	754
Natural gas, land tenures & minerals	842	1,018	949	1,188	1,130	1,594
Water and other resources	579	576	574	610	576	589
Total Natural Resource Revenue	**2,413**	**2,586**	**2,413**	**2,711**	**2,571**	**2,937**
Medical services plan premiums	1,361	2,264	2,248	2,558	2,434	2,254
Other fees and licences	4,002	3,928	3,814	3,655	3,402	3,171
Investment earnings 1	276	297	272	260	293	315
Other revenue	3,060	3,094	2,945	2,966	2,943	2,735
B.C. Liquor Distribution Branch	1,106	1,101	1,095	1,083	1,031	935
B.C. Hydro and Power Authority	448	897	635	995	180	(153)
B.C. Lottery Corporation	1,300	1,365	1,301	1,329	1,304	1,245
Earnings from other government business enterprises	(560)	(1,204)	(140)	(578)	(286)	605
Total Own-Source Revenue	**43,998**	**42,552**	**42,763**	**42,072**	**38,198**	**37,100**
Canada Health & Social Transfer	6,921	6,691	6,672	6,495	6,149	5,827
Other federal transfers	2,009	1,857	1,700	1,672	1,498	1,452
Total Federal Transfer Payments	**8,930**	**8,548**	**8,372**	**8,167**	**7,647**	**7,279**
DBRS-Adjusted Revenues	**52,928**	**51,100**	**51,135**	**50,239**	**45,845**	**44,379**
Expenditures						
Health	21,651	20,819	20,747	19,689	19,203	18,370
Education	13,897	13,291	13,376	12,468	12,212	11,827
Social services	5,317	4,723	4,745	4,243	4,106	3,847
Protection of persons and property	1,650	1,916	1,830	1,655	1,572	1,451
Natural resources & economic development	2,433	2,892	2,720	2,504	2,477	2,191
Transportation	2,134	2,019	2,068	1,784	1,670	1,608
Other 2	2,367	2,243	2,235	2,260	1,264	1,288
General government	1,436	1,337	1,465	1,532	1,501	1,359
Capital assets bought less amortized 3	2,831	1,903	2,672	1,021	1,256	1,250
DBRS-Adjusted Program Expenditures	**53,716**	**51,143**	**51,858**	**47,156**	**45,261**	**43,191**
Total taxpayer-supported interest costs 4	1,849	1,699	1,776	1,657	1,899	1,663
Less sinking fund earnings	(13)	(15)	(12)	(52)	(34)	(25)
Net Interest Costs	**1,836**	**1,684**	**1,764**	**1,605**	**1,865**	**1,638**
DBRS-Adjusted Expenditures	**55,552**	**52,827**	**53,622**	**48,761**	**47,126**	**44,829**
DBRS-Adjusted Surplus (Deficit)	**(2,624)**	**(1,727)**	**(2,487)**	**1,478**	**(1,281)**	**(450)**
DBRS adjustments						
Non-recurring revenue (expenditures) 5	98	274	298	549	361	130
B.C. Hydro adjustment	264	(199)	63	(311)	475	734
Capital assets bought less amortized 3	2,831	1,903	2,672	1,021	1,256	1,250
Forecast allowance	(350)	(100)	(300)	-	-	-
Surplus (Deficit), as Reported	**219**	**151**	**246**	**2,737**	**811**	**1,664**

1 Excludes sinking fund earnings, which are netted against interest charges. 2 Includes expense contingencies. 3 Acquired capital assets are amortized over their useful lives; this adjustment converts amortization to pay-as-you-go tax-supported capital spending. 4 Includes the interest portion of debt service grants for schools, hospitals, universities and transit/SkyTrain that are included in CRF program spending. 5 Includes release of surplus assets in 2013–14 through 2016–17.

Statement of Financial Position (DBRS-Adjusted)

($ millions)	As at March 31 2019	2018	2017	2016	2015	2014	2013	2012
Public Sector Debt 1								
Provincial direct debt	22,766	23,190	25,653	27,796	27,920	27,892	26,244	23,698
Economic development debt	17,781	16,393	12,249	11,465	10,725	10,229	9,421	8,644
Other guaranteed debt 2	4,651	4,097	3,604	3,466	3,235	2,947	2,517	2,317
Net Tax-Supported Debt (Per Province)	**45,198**	**43,680**	**41,506**	**42,727**	**41,880**	**41,068**	**38,182**	**34,659**
Net municipal debt (non-guaranteed) 3	5,168	4,693	4,373	4,288	4,299	4,376	4,341	4,207
Net Tax-Supported Debt (DBRS Adjusted)	**50,366**	**48,373**	**45,879**	**47,015**	**46,179**	**45,444**	**42,523**	**38,866**
Self-supporting Crown corporations:								
B.C. Hydro & Power Authority	22,541	20,239	19,692	17,928	16,544	15,559	14,167	12,978
B.C. Lotteries, Columbia Power & others	1,283	1,245	1,255	1,248	1,161	857	857	777
Transportation Investment Corporation	0	0	3,430	3,389	3,335	3,209	2,610	1,779
Total Public-Sector Net Debt	**74,190**	**69,857**	**70,256**	**69,580**	**67,219**	**65,069**	**60,157**	**54,400**
Unfunded pension liabilities	187	187	187	246	261	214	165	110
DBRS-Adjusted Debt								
Per capita	10,384	10,081	9,682	10,067	9,995	9,947	9,390	8,663
As a share of GDP	17.3%	17.4%	17.5%	18.8%	19.2%	19.9%	19.3%	18.0%
Gross Debt Breakdown by Currency 4								
CAD pay	100%	100%	100%	100%	100%	100%	100%	99%
Non-CAD pay	0%	0%	0%	0%	0%	0%	0%	1%
Fixed-/Floating-Rate Breakdown 4, 5								
Fixed rate	82%	80%	82%	79%	78%	73%	80%	81%
Floating rate	18%	20%	18%	21%	22%	27%	20%	19%

Debt Maturity Profile 4, 6	2017–18	2018–19	2019–20	2020–21	2021–22	2022–23	2023–24 to 2027–28	2028–29+	Total
Tax-supported debt ($ millions)	2,090	2,688	2,652	1,909	3,365	3,825	9,203	17,859	43,591
Tax-supported debt (%)	4.8%	6.2%	6.1%	4.4%	7.7%	8.8%	21.1%	41.0%	100.0%

1 Debt numbers are reported net of sinking fund assets and pre-financing. 2 Includes tax-supported Crown corporations and agencies, other fiscal agency loans and various loan guarantees. 3 December year end. Net of sinking fund assets and other liquid marketable securities. 4 All amounts are net of hedges (if any). Excludes municipal debt. 5 Includes all debt that matures or is repriced within 12 months. 6 Debt maturity profile is as at the budget date of March 31, 2017.

Rating History

	Current	2017	2016	2015	2014	2013
Issuer Rating	AA (high)	AA (high)	AA (high)	AA (high)	AA (high)	AA (high)
Long-Term Debt	AA (high)	AA (high)	AA (high)	AA (high)	AA (high)	AA (high)
Renminbi Bonds	AA (high)	AA (high)	AA (high)	NR	NR	NR
Short-Term Debt	R-1 (high)	R-1 (high)	R-1 (high)	R-1 (high)	R-1 (high)	R-1 (high)

Previous Action

- Assigned, November 23, 2017.

Related Research

- *2018 Provincial Government Fact Sheet*, April 2, 2018.
- *Corporate Risk Assessment Scorecard for Canadian Provincial Governments*, April 2, 2018.
- *British Columbia's 2018 Budget: Following through on campaign commitments*, February 21, 2018.
- "DBRS Comments on the British Columbia Government's Decision to Complete Site C Construction," December 12, 2017.
- *Rating Canadian Provincial Governments*, May 2017.
- *Rating Canadian Provincial Agents of the Crown*, May 2017.
- British Columbia Hydro and Power Authority: Rating Report, January 5, 2018.

Previous Report

- British Columbia, Province of: Rating Report, October 26, 2017.

Notes:
All figures are in Canadian dollars unless otherwise noted.

For the definition of Issuer Rating, please refer to Rating Definitions under Rating Policy on www.dbrs.com.

Generally, Issuer Ratings apply to all senior unsecured obligations of an applicable issuer, except when an issuer has a significant or unique level of secured debt.

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