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# Announcement: Moody's notes that balanced budget forecasts allow for increased social spending in the first budget of British Columbia's new government

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Toronto, September 12, 2017 -- Moody's Investors Service notes that a strong provincial economy and new revenue initiatives will support increased spending and higher debt in the first budget of the Province of British Columbia's (Aaa stable) newly formed government. The budget, with 3-year forecasts for the 2017/18 to 2019/20 fiscal years, was presented as an update to the previous government's February 2017 budget plan.

"Despite the government's commitment to large social spending initiatives, the budget forecasts continued surpluses across the 3-year budget horizon backed by a strong provincial economy. Nonetheless, surpluses will remain thin after including contingencies and forecast allowances, averaging only CAD244 million annually over the next three years (between 0.4% and 0.5% of revenue)," noted Adam Hardi, Moody's Assistant Vice President. The province closed the most recent fiscal year for 2016/17 with a sizeable surplus of CAD2.7 billion, equivalent to 5.3% of revenue.

Revenues are forecasted to grow to CAD52.4 billion in 2017/18, up 1.8% relative to 2016/17. Revenue forecasts include a mix of previously announced and new measures supported by a number of tax initiatives, including the introduction of a new tax bracket for high income earners, raising the corporate income tax by 1 percentage point, and increasing carbon taxes. These measures will be partly offset by lower revenues from declining natural resource revenues, the removal of bridge tolls, and lower medical plan premiums.

Revenue growth will also be supported by a strong economy. The province forecasts that real GDP grew 3.6% in 2016, and will increase 2.9% in 2017, exceeding the levels anticipated in the February budget (3.0% and 2.1%, respectively) backed by low unemployment rates, strong housing activity (despite recent moderation) and continued solid export activity. The expected growth rates for 2018 and 2019 were left unchanged at 2.1% and 2.0%. As with previous budgets, the province's forecasts are conservative relative to the outlook provided by the Economic Forecast Council.

The natural resource sector is expected to remain weak in the face of continued low prices for natural resources. In addition, potential disruptions to softwood lumber exports from possible U.S. protectionist measures and the NAFTA renegotiation remain risks for the province. The province accounts for the potential negative impact of these risks through its risk contingencies.

On the expenditure side, the province forecasts a sharp increase in expenditures of 6.4% in 2017/18 relative to the 2016/17 fiscal year. The increased expenses reflect previously identified measures in addition to the new government's social spending priorities in the education, healthcare and housing sectors and poverty reduction. The increased spending also includes considerable costs incurred to fight forest fires this year. Across the 3-year budget horizon, expenditures will increase by an aggregate CAD1.8 billion relative to the February budget. While the spending increases will be supported by anticipated higher revenues, Moody's notes that the outer years of the 3-year budget horizon call for lower growth rates, which may be challenging to achieve given the government's elevated spending priorities.

Capital spending across the 2017/18 -- 2019/20 budget horizon is expected to total CAD23.1 billion, lower than the CAD24.5 billion envisioned in the February budget. Of this amount, CAD11.7 billion will come from new borrowing. Moody's expects that the province's net direct and indirect debt relative to revenues could exceed 90%, slightly above Moody's previous forecast range of 85-90% of revenue, and will continue to place British Columbia's debt burden among the highest of Moody's-rated Aaa regional governments.

"Given modest revenue growth, ongoing borrowing for capital spending, and the reclassification of CAD3.5 billion in obligations to taxpayer-supported debt following the elimination of bridge tolls, the province's debt burden will remain elevated," said Mr. Hardi.

As part of its normal monitoring practice, Moody's will evaluate the 2017/18 budget update's assumptions and its potential for upside and downside risks within the context of likely impacts on the province's debt burden.

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