

**CREDIT OPINION**

20 September 2024

Update

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**RATINGS**

**British Columbia, Province of**

Domicile	British Columbia, Canada
Long Term Rating	Aaa
Type	LT Issuer Rating
Outlook	Negative

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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# Province of British Columbia (Canada)

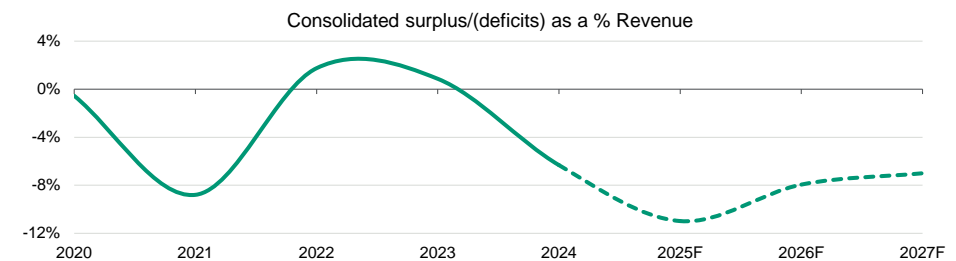
## Update to credit opinion

**Summary**

The credit profile of the [Province of British Columbia](#) (Aaa negative) reflects a large economy with a diversified sector base, and a stable and mature institutional framework, with the ability to access a wide range of revenue sources and alter spending plans. The institutional framework also provides the province with important federal fiscal funding, including health and social transfers. The province maintains strong wealth metrics although compared to peers the liquidity ratio is low given that much of its wealth is held in long-term investments. Key pressures come from large deficits over the next three years, driven by a combination of slower than historical near-term economic growth and increased spending needs, with no commitment to return to fiscal balance within a specified period. Rising spending will result in a sustained debt increase in the absence of significant mitigation efforts.

Exhibit 1

**Rising spending and slow economic growth contribute to large and protracted deficits (fiscal years ending March 31)**



Sources: Province of British Columbia and Moody's Ratings

**Credit strengths**

- » Sector diversity and tax competitiveness support economic resilience
- » Well-established institutional framework provides significant policy flexibility
- » Significant liquidity support from cash and investments, but declining from recent high levels

**Credit challenges**

- » Prioritizing spending initiatives pushes up spending and results in structural deficits
- » Material rise in the debt burden weakens debt affordability and reduces fiscal flexibility

## Rating outlook

The negative outlook reflects the risks to the province's ability to slow a significant projected increase in debt amid rising spending commitments and its lack of commitment to return to fiscal balance within a specified period. The province's increased spending focus on social infrastructure and services, including healthcare and education, could result in a sustained debt increase in the absence of significant mitigation efforts.

## Factors that could lead to an upgrade

The outlook could be stabilized if the province demonstrated significant new spending controls, which along with a faster increase in revenues could support a return to balance within a relatively quick timeline. New mitigating strategies that limit debt growth and preserve liquidity would also contribute to stabilising the outlook.

## Factors that could lead to a downgrade

The rating could be downgraded if the province is unable to meaningfully improve its fiscal trajectory over the next 12-18 months, resulting in material deficits. A clear indication that debt will rise materially in line with current projections, or substantially weaker liquidity metrics would also result in downward pressure.

## Key indicators

Exhibit 2

### Province of British Columbia

(Year Ending March 31)	2022	2023	2024	2025F	2026F	2027F
Net Direct and Indirect Debt as a % of Revenue	118.5	104.1	129.1	151.3	173.2	192.5
Net Direct and Indirect Debt as a % of GDP	24.1	21.5	25.1	29.2	33.0	36.2
Cash Financing Surplus (Requirement) as a % of Revenue	(2.8)	4.1	(21.4)	(23.2)	(20.4)	(18.6)
Consolidated Surplus (Deficit) as a % of Revenue	1.7	0.9	(6.3)	(11.0)	(7.9)	(7.0)
Adjusted Interest Expense as a % of Revenues	2.6	2.5	3.0	3.7	4.4	5.2
Intergovernmental Transfers as a % of Revenue	16.5	15.4	17.2	17.8	17.8	17.0
Real GDP Growth (%) [1]	3.8	1.6	1.0	2.0	2.3	2.3

(1) Corresponds to calendar year

Sources: Province of British Columbia and Moody's Ratings

## Detailed credit considerations

### Baseline credit assessment

The credit profile of the Province of British Columbia, as expressed in its Aaa negative rating, combines a baseline credit assessment (BCA) for the province of aa1, and a high likelihood of extraordinary support coming from the [Government of Canada](#) (Aaa stable) in the event that the province faced acute liquidity stress.

### Sector diversity and tax competitiveness support economic resilience

British Columbia is the third largest Canadian province by population and fourth largest provincial economy, accounting for around 14% of Canada's GDP. Located on Canada's western coast, British Columbia remains an important hub for goods shipped to and from Asia, and as a result the export markets of British Columbia are more diversified than Canada and other provinces, a key credit strength.

The province's real GDP growth slowed to 1.6% in 2023 following significantly stronger growth of 3.8% in 2022. Further slowdown is projected with a growth rate of 1.0% in 2024, largely reflecting high levels of inflation which weighs on costs, tighter monetary conditions and overall slower growth across many of its major trading partners. Based on its first quarter 2024-25 fiscal update released in September 2024, the province projects real GDP growth to return to long-term stable levels of 2.0% in 2025 and 2.3% in 2026 as inflation eases and global demand recovers.

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While Canada typically sees nearly three-quarters of exports flow to the US, the US accounts for approximately only half of British Columbia's exports. Other key markets include China and Japan and several other countries in the Asia-Pacific region. The significance of China in the province's Asian exports exposes the province to some concentration risk, although the wide diversification of sectors and markets reduces vulnerability from sector or trading partner-specific shocks.

Economic diversity is underpinned by several large industries including real estate, wholesale and retail trade, tourism and construction. The economy provides for a large tax base which ensures that provincial revenues are not strongly impacted by a decline in one particular sector. Furthermore, British Columbia's level of taxation is at the lower end of the Canadian provinces, providing flexibility to raise taxes if necessary while still remaining competitive with other jurisdictions. These factors support the province's attractiveness to businesses and individuals, and also contribute to strong international immigration.

This economic strength is also supported by an important natural resources sector, primarily natural gas and forestry products, and we expect that increased global demand for Canadian resources will further support the province's natural resources sector. Approximately CAD40 billion in new upstream, pipeline and liquefaction plant construction projects in the province by LNG Canada, a consortium of international energy companies, and [TC Energy Corp.](#) (Baa3 stable) will provide support to the natural gas industry.

### **Well-established institutional framework provides significant policy flexibility**

British Columbia, like most Canadian provinces, enjoys significant flexibility in its financial management. The institutional framework governing relations, powers and responsibilities between the Canadian provinces and the federal government is well developed and stable. The province's capacity to respond to pressures is supported by a stable and mature institutional framework for Canadian provinces, which allows unfettered access to a wide range of revenue measures as well as the ability to alter spending plans.

Compared to their counterparts in other countries, including the German Länder and the Australian states, Canadian provinces enjoy far greater fiscal and budgetary autonomy. As a result, British Columbia benefits from a high degree of fiscal policy flexibility that is more similar to sovereign governments than many international sub-sovereign peers. These positive institutional factors increase the province's ability to manage through economic downturns and handle higher debt burdens.

The institutional framework also includes important federal fiscal transfers to the province, including gradually rising health and social transfers. These transfers are highly predictable and secure, and therefore largely unaffected by economic changes. The province projects federal transfers to account for around 18% of British Columbia's total revenues for 2024-25, largely in line with historical levels. The provincial healthcare sector will also benefit from increased federal health transfers over the next 10 years, under a combined CAD27 billion funding agreement in principle.

### **Significant levels of cash and investments, but declining from recent high levels**

We view the province's wealth metrics as strong, with combined cash (including cash equivalents) and investments totalling CAD12 billion at March 31, 2024 and covering 11.7% of net direct and indirect debt and 14.2% of total expenses. Following a buildup of a significant liquidity cushion during the pandemic years to provide a buffer against fiscal pressures, we project wealth levels to revert to more stable but still robust long-term levels of around CAD10 billion over the next three years, as the province will draw down part of its reserves to fund a portion of the capital plan and to address operating needs.

Cash and investments also provide a buffer for bondholders against fiscal shortfalls and rising expenses including debt costs. The province also maintains significant credit facilities for liquidity management, if needed, including a CAD500 million uncommitted and a CAD2.5 billion committed credit facility with Canadian banks.

Given that much of the province's wealth is held in long-term investments, the liquidity ratio (cash and cash equivalents as a % of operating revenue) at 7.9% at March 31, 2024 is at the low end relative to provincial peers. We project that the liquidity ratio will weaken modestly as debt levels continue to rise and expenses remain elevated, but stabilize at around 5-6% over the next three years.

### **Prioritizing spending initiatives pushes up spending and results in structural deficits**

The province forecasts large and persistent deficits, averaging CAD7.3 billion, or 8.6% of revenue, over 2024-25 to 2026-27 based on its first quarter 2024-25 fiscal update released in September 2024. This follows a deficit of CAD5.0 billion, or 6.3% of revenue, for

2023-24. Although the projections contain significant contingencies, which account for between 40% and 60% of deficits and provide a buffer to the forecasts, we view these deficits as structural in nature, especially given the lack of clarity by the government on a path back to balance.

The deficits reflect a combination of slower economic growth and continued higher than historical interest rates despite the Bank of Canada's recent interest rate cuts. As a result, and given the province's large borrowing program for the next three years, debt and refinancing costs will continue to rise. Expenses are further pressured by elevated costs, global supply chain disruptions and labour scarcity which put upward pressure on both operating and capital spending. Spending will increase across the key areas of health (41% of revenue), education (22%) and social services (11%), outpacing projected revenues by a significant margin and contributing to ongoing deficits.

In line with provincial projections, we estimate total expense for 2024-25 at CAD90.7 billion, 7.2% higher than 2023-24. Spending priorities focus strongly on improving overall affordability, rental protection and one-time affordability credits, with spending continuing to rise over the three-year budget horizon.

The increase in the severity and frequency of weather-related events including floods and wildfires – as evidenced by significant wildfires in 2023 and year-to-date 2024 – creates additional challenges. Although the province has comprehensive response plans for these events, the uncertainty regarding timing and magnitude of weather events could further impair the province's fiscal trajectory and its plans to return to balance given the considerable costs of fire suppression. A partial mitigant to these costs comes from the federal government's natural disaster assistance arrangement.

### **Material rise in the debt burden weakens debt affordability and reduces fiscal flexibility**

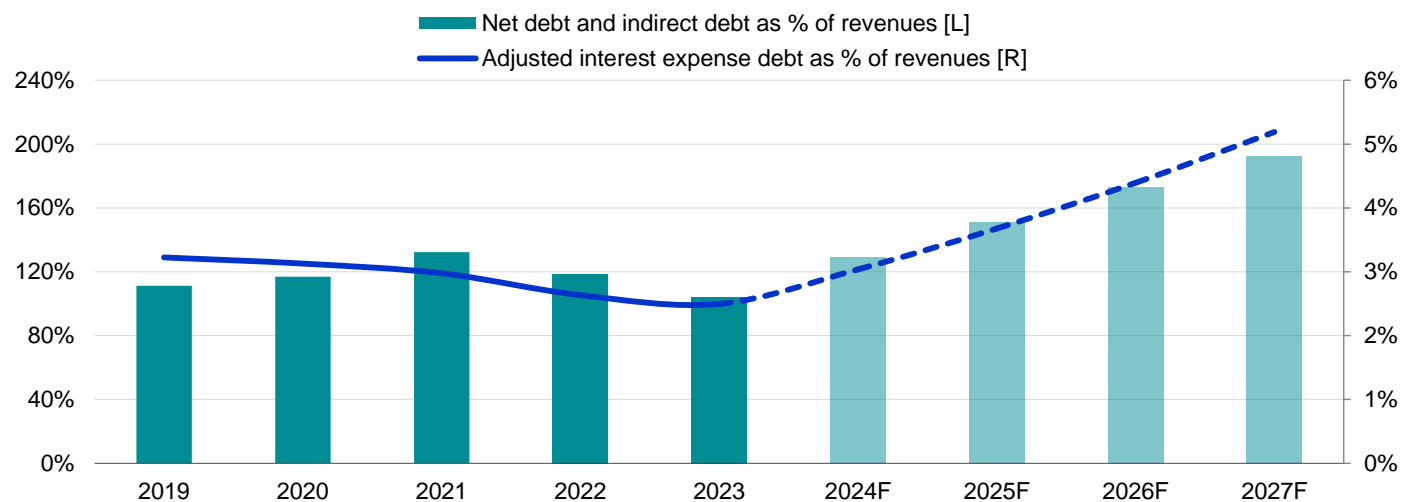
Although historically the province maintained lower debt burdens than Canadian provincial peers, the need to finance operating deficits, as well as the province's large-scale capital spending program, puts upward pressure on debt levels. The three year capital plan totals CAD56.9 billion for 2024-25 to 2026-27, 16% higher than the 3-year capital spending in last year's budget. As a result, the province's debt financing needs will increase materially, leading to a faster rise in debt burden compared to our previous forecasts.

The province's aggregate borrowing program, which includes financing of both capital spending and deficits, will increase by approximately CAD61 billion over the next three years. Net direct and indirect debt, which includes the debt issued by the province on behalf of [British Columbia Hydro and Power Authority](#) (BC Hydro, Aaa negative), the provincially owned utility company, could reach CAD167.6 billion by 2026-27, and as a result we project that the debt burden could exceed 190% by 2026-27, up from 104% in 2022-23. Despite the recalibration of the debt burden under our updated methodology, our credit considerations remain unchanged that BC Hydro will continue to service its debt without liquidity or other operating support from the province.

The large and increasing borrowing program over multiple years will result in an increasing interest burden, eroding some of the province's historically very high debt affordability given the continued higher than historical level of interest rates. As a result, we expect that if the debt burden rises in line with budget projections, the interest burden will rise to 5.2% by 2026-27 from 3.0% in 2023-24.

Exhibit 3

**The rapid rise in the debt burden reflects debt financing of both projected deficits and capital spending**  
(Fiscal years ending March 31)



Sources: Province of British Columbia and Moody's Ratings

BC Hydro forms a significant portion of debt issued by the province. While BC Hydro generates a steady revenue stream with sufficient cash flow to support operations, its total reported debt has consistently risen in recent years and currently constitutes approximately 30% of the province's total debt in 2023-24. BC Hydro's largest current project is the Site C hydroelectric dam. Following earlier cost escalations, Site C construction is winding down which will provide relief from further spending and debt escalation for this project.

**Extraordinary support considerations**

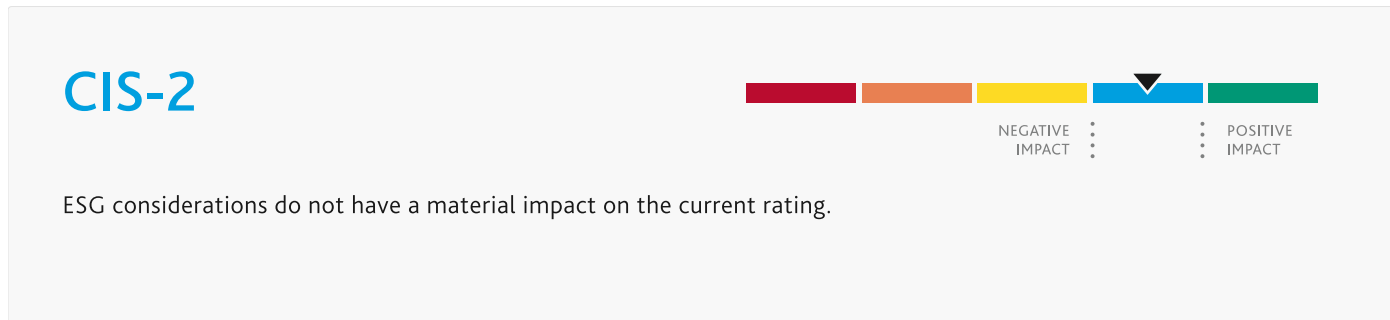
We consider that there is a high likelihood that British Columbia would receive extraordinary support from the Government of Canada should the province experience an acute liquidity need. This reflects our assessment of the incentive to the federal government of minimizing the risk of potential disruptions to capital markets if British Columbia, or any province, were to default, as well as indications of a moderately positive federal government policy stance, as illustrated by the flexibility inherent in the system of federal-provincial transfers.

## ESG considerations

British Columbia, Province of's ESG credit impact score is CIS-2

Exhibit 4

### ESG credit impact score



Source: Moody's Ratings

The **CIS-2** indicates that ESG considerations do not have a material impact on the current rating.

Exhibit 5

### ESG issuer profile scores



Source: Moody's Ratings

### Environmental

The environmental issuer profile score (IPS) of **E-3** reflects exposure to weather events including frequent occurrence of flooding and large wildfires which create economic damage. However, provincial budgets contain contingencies for weather-related expenses, and benefits from federal disaster recovery assistance. The province also has significant green initiatives and very strong environmental protection policies, supported by measurable and important targets relating to climate action and accountability, including greening of its transit fleet and a target of achieving net-zero carbon emissions by 2050.

### Social

The social IPS of **S-2** indicates strong health and safety measures and high liveability which is a significant draw for international immigration, boosting economic activity. Labour and income trends are solid, although social pressures, especially relating to healthcare and housing supply and home affordability challenges add negative credit pressure on operating and capital spending.

### Governance

The governance IPS of **G-2** reflects very strong governance attributes with forward-looking multi-year planning and transparent reporting and disclosure, although less robust overall risk controls and financial management than under Moody's previous assessment.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

## Rating methodology and scorecard factors

The assigned BCA of aa1 is close to the BCA scorecard-indicated outcome of aa2. For details of our rating approach, please refer to [Regional and Local Governments](#) published May 2024.

Exhibit 6

### British Columbia, Province of Regional & Local Governments

Baseline Credit Assessment – Scorecard	Score	Value	Sub-factor Weighting	Sub-factor Score	Factor Weighting	Total
<b>Factor 1: Economy</b>					<b>25%</b>	<b>0.96</b>
Regional Income [1]	2.39	59967.95	15%	0.36		
Economic Growth	9.00	baa	5%	0.45		
Economic Diversification	3.00	aa	5%	0.15		
<b>Factor 2: Institutional Framework and Governance</b>					<b>30%</b>	<b>0.30</b>
Institutional Framework	1.00	aaa	15%	0.15		
Governance	1.00	aaa	15%	0.15		
<b>Factor 3: Financial Performance</b>					<b>20%</b>	<b>1.86</b>
Operating Margin [2]	12.22	0.41%	10%	1.22		
Liquidity Ratio [3]	11.75	7.92%	5%	0.59		
Ease of Access to Funding	1.00	aaa	5%	0.05		
<b>Factor 4: Leverage</b>					<b>25%</b>	<b>2.02</b>
Debt Burden [4]	8.45	129.09%	15%	1.27		
Interest Burden [5]	7.56	3.04%	10%	0.76		
<b>Preliminary BCA Scorecard-Indicated Outcome (SIO)</b>						<b>(5.14) a1</b>
<b>Idiosyncratic Notching</b>						<b>1.0</b>
<b>Preliminary BCA SIO After Idiosyncratic Notching</b>						<b>(4.14) aa3</b>
<b>Sovereign Rating Threshold</b>						<b>Aaa</b>
<b>Operating Environment Notching</b>						<b>1.0</b>
<b>BCA Scorecard-Indicated Outcome</b>						<b>(3.14) aa2</b>
<b>Assigned BCA</b>						<b>aa1</b>

[1] Regional GDP per capita in terms of purchasing power parity (PPP) terms, in international dollars

[2] Primary Operating Balance / Operating Revenue

[3] Cash and Cash Equivalents / Operating Revenue

[4] Net Direct and Indirect Debt / Operating Revenue

[5] Interest Payments / Operating Revenue

Source: Moody's Ratings; Fiscal 2023.

## Ratings

Exhibit 7

Category	Moody's Rating
<b>BRITISH COLUMBIA, PROVINCE OF</b>	
Outlook	Negative
Baseline Credit Assessment	aa1
Issuer Rating	Aaa
Senior Unsecured	Aaa
Commercial Paper	P-1

Source: Moody's Ratings

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