

## British Columbia: 2018–19 Q2 Update

### SUMMARY

- The Province of British Columbia published its Second Quarterly Report (*Report*) for fiscal year 2018–19 (FY19) on Monday.
- The *Report* outlined a budgetary surplus of \$1.35 bn<sup>1</sup> for this fiscal year, \$681 mn higher than forecast as of Q1-2018.
- A stronger revenue profile is expected to dominate modest upward revisions to expenditures and additional contingencies to mitigate potential downside risks.
- BC's taxpayer-supported debt is projected to come in \$2.3 bn lower than forecast in Q1. This would eliminate the Province's operating debt.

### ECONOMIC CONDITIONS

**BC continues to base its fiscal planning on economic growth of 2.2% in 2018 and 1.8% in 2019 despite modest shifts in private sector forecasts.** In keeping with longstanding practice, it incorporated growth lower than the private sector average into its fiscal plan (chart 1, p.2). It also noted improvements since the Q1 forecast for employment, manufacturing shipments, nominal exports, building permits and interprovincial migration.

**The housing market outlook was little changed.** New home construction remains buoyant so far this year, and the resulting upswing in new listings continues to exert downward pressure on purchase prices. Home sales remain soft relative to the elevated levels of the last two years but look to be adjusting to new housing regulations plus rising interest rates in H2-2018.

**With respect to trade, the *Report* identified a number of downside risks.** The global rise of protectionism and the prospect of slowing growth in Asia is consequential for BC in particular given its strong trade ties to the continent. Weaker economic growth related to the UK's exit from the European Union poses similar challenges. The softwood lumber dispute and recent declines in Western spruce-pine-fir prices from more than USD 600 mbfm in June to less than USD 400 mbfm in October (chart 2, p.2) represent further concerns for one of BC's key exports.

### FISCAL PROJECTIONS

**Total revenue is forecast to register gains \$1.4 bn higher than planned in the Q1 update.** Key to the revision are one-time prior-year adjustments to personal and corporate income tax receipts, which are expected to contribute to a \$1.6 bn windfall. These gains are forecast to be eroded by: lower property transfer tax receipts (reflecting the housing market soft patch); weaker federal government contributions; and softer Crown corporation net incomes. This last revision is dominated by a fall relative to Q1 of more than \$200 mn for the Insurance Corporation of BC (ICBC).

### CONTACT

**Marc Desormeaux, Provincial Economist**  
 416.866.4733  
 Scotiabank Economics  
[marc.desormeaux@scotiabank.com](mailto:marc.desormeaux@scotiabank.com)

### Updated Fiscal Forecast

\$ millions except where noted

	FY18	FY19	
	Final	Q1	Q2
Tax Revenue	28,321	31,383	32,829
Natural Resource Revenue	2,695	2,908	2,959
Commercial Crown Corp. Net Inc.	1,056	2,627	2,412
Other Own-Source Revenue	10,893	9,776	9,901
<b>Total Own-Source Revenue</b>	<b>42,965</b>	<b>46,694</b>	<b>48,101</b>
Federal Transfers	9,055	9,121	9,097
<b>Total Revenue</b>	<b>52,020</b>	<b>55,815</b>	<b>57,198</b>
Health	20,927	21,684	21,731
Education, K-12 & Post-Secondary	13,091	14,094	14,069
Social Services	4,737	5,319	5,310
Other Program Spending	10,341	11,045	11,148
<b>Program Spending</b>	<b>49,096</b>	<b>52,142</b>	<b>52,258</b>
Debt Service*	2,623	2,654	2,640
<b>Total Expenditure</b>	<b>51,719</b>	<b>54,796</b>	<b>54,898</b>
Forecast Allowance	0	350	950
<b>Surplus</b>	<b>301</b>	<b>669</b>	<b>1,350</b>
<b>Capital Outlays:</b> Taxpayer-Supp.	3,908	5,579	5,177
Self-Supported	2,729	4,078	4,061
<b>Taxpayer-Supported Debt</b>	<b>43,607</b>	<b>44,717</b>	<b>42,431</b>
<b>Annual Change, %</b>			
Tax Revenue	4.5	10.8	15.9
Natural Resource Revenue	-0.6	7.9	9.8
<b>Total Own-Source Revenue</b>	<b>-0.7</b>	<b>8.7</b>	<b>12.0</b>
Federal Transfers	10.9	0.7	0.5
<b>Total Revenue</b>	<b>1.1</b>	<b>7.3</b>	<b>10.0</b>
Health	6.3	3.6	3.8
Education	5.0	7.7	7.5
Social Services	11.6	12.3	12.1
Other Program Spending	6.2	6.8	7.8
<b>Program Spending</b>	<b>6.4</b>	<b>6.2</b>	<b>6.4</b>
<b>Total Expenditure</b>	<b>6.2</b>	<b>5.9</b>	<b>6.1</b>
<b>Memo Items, %</b>			
Own-Source Revenue / GDP	15.2	15.8	16.2
Program Spending / GDP	17.4	17.6	17.6
Total Expenditure / GDP	18.3	18.5	18.5
Budget Balance/ GDP	0.1	0.2	0.5
Taxpayer-Supported Debt / GDP	15.5	15.1	14.3
Taxpayer-Supp. Debt / Revenue	83.8	80.1	74.2
Debt Service* / Revenue	5.0	4.8	4.6

\* Taxpayer-supported basis. Sources: BC Finance, Statistics Canada; nominal GDP forecasts: Scotiabank Economics.

<sup>1</sup> Figures reported in Canadian dollars unless otherwise stated.

**Total expenditure is projected to come in \$102 mn higher than anticipated in the prior projection.** Spending on fire and flood management services is expected to be \$160 mn higher than the Q1 forecast. The Province also foresees higher operating costs related to post-secondary education. Reduced refundable tax credit payments of \$118 mn—2017 tax return data revealed lower effective rates will likely apply to film & television production in calendar year 2018—counteract these outlays alongside lower debt servicing costs. Details of the costs associated with wage increases for unionized public sector employees, set to be awarded after BC's real economic growth diverged from the Budget 2018 forecast, will be provided in the 2019 Budget.

**To mitigate trade- and housing-related downside, the Province upped its forecast allowance by \$600 mn.** Contingencies of \$950 mn are now earmarked for FY19.

**For capital spending, the key development was a \$402 mn reduction since Q1 in the forecast for taxpayer-supported outlays.** Adjustments to the timing of previously planned expenditures, notably on the Broadway Subway project, are the proximate cause. Ventures now incorporated into fiscal planning include a \$79 mn high school in Burnaby, a \$54 mn elementary school in Chilliwack, a \$63 mn expansion of Highway 1 from Kamloops to Alberta and an \$81 mn strategic property purchase in Vancouver. The *Report* also notes modest cost reductions on two dam projects, delays on a mental health and addiction treatment facility in Burnaby and the completion of a post-secondary arts & design campus redevelopment.

**The *Report's* pièce de résistance was the projected elimination of provincial operating debt for the first time in four decades.** The reduction in taxpayer-supported debt since Q1 mirrors a \$2.1 bn increase in cash originating from the larger-than-anticipated surplus and lower capital spending profile. To align with the \$950 mn forecast contingency, BC is building an equivalent borrowing allowance into its fiscal blueprint.

## OUR TAKE

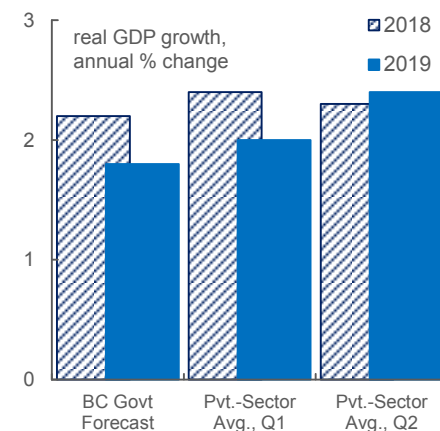
**One-time events drove much of the change to the bottom line, but BC maintains one of the most favourable financial positions of any province in Canada.** The province's expansion is at an advanced stage and near-term risks are nontrivial. Yet conservative GDP forecasts and a sizeable contingency reserve should serve as a bulwark against adverse economic shocks.

**Given the stronger surplus, lighter debt load and the possibility that growth will outpace the Province's forecast in FY19, we view further pocketbook relief as a likely outcome of the next BC Budget scheduled for February 19, 2019.** Improving affordability has thus far been a priority for the Government and the better fiscal position leaves room to bolster steps already taken and announced in areas such as child care and prescription drug costs.

**An important question going forward is how the \$40 bn LNG Canada project will impact fiscal planning in the outer years of the forecast period.** Our forecast assumes Canada's largest-ever private-sector project will generate capital expenditures of nearly \$14 bn during 2019–20 that will propel BC's economic growth well above that of the other provinces. In line with industry estimates of capital spending profiles for comparable projects, peak construction is expected in 2021 with workforce ramp-up about 18 months after the October 2018 final investment decision. For details on the Government's economic forecast and the anticipated timing of future personal and income tax receipts, we await the 2019 Budget.

Chart 1

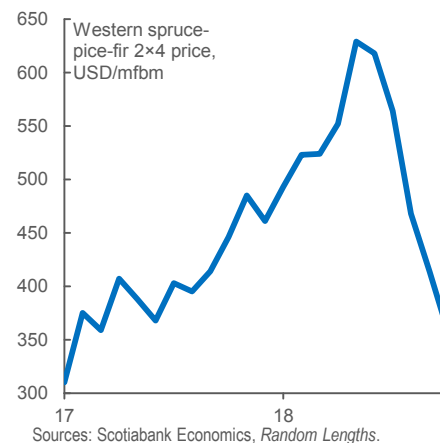
### Building in Fiscal Prudence



Sources: Scotiabank Economics, BC Finance.

Chart 2

### Plunging Lumber Prices



Sources: Scotiabank Economics, Random Lengths.

This report has been prepared by Scotiabank Economics as a resource for the clients of Scotiabank. Opinions, estimates and projections contained herein are our own as of the date hereof and are subject to change without notice. The information and opinions contained herein have been compiled or arrived at from sources believed reliable but no representation or warranty, express or implied, is made as to their accuracy or completeness. Neither Scotiabank nor any of its officers, directors, partners, employees or affiliates accepts any liability whatsoever for any direct or consequential loss arising from any use of this report or its contents.

These reports are provided to you for informational purposes only. This report is not, and is not constructed as, an offer to sell or solicitation of any offer to buy any financial instrument, nor shall this report be construed as an opinion as to whether you should enter into any swap or trading strategy involving a swap or any other transaction. The information contained in this report is not intended to be, and does not constitute, a recommendation of a swap or trading strategy involving a swap within the meaning of U.S. Commodity Futures Trading Commission Regulation 23.434 and Appendix A thereto. This material is not intended to be individually tailored to your needs or characteristics and should not be viewed as a “call to action” or suggestion that you enter into a swap or trading strategy involving a swap or any other transaction. Scotiabank may engage in transactions in a manner inconsistent with the views discussed this report and may have positions, or be in the process of acquiring or disposing of positions, referred to in this report.

Scotiabank, its affiliates and any of their respective officers, directors and employees may from time to time take positions in currencies, act as managers, co-managers or underwriters of a public offering or act as principals or agents, deal in, own or act as market makers or advisors, brokers or commercial and/or investment bankers in relation to securities or related derivatives. As a result of these actions, Scotiabank may receive remuneration. All Scotiabank products and services are subject to the terms of applicable agreements and local regulations. Officers, directors and employees of Scotiabank and its affiliates may serve as directors of corporations.

Any securities discussed in this report may not be suitable for all investors. Scotiabank recommends that investors independently evaluate any issuer and security discussed in this report, and consult with any advisors they deem necessary prior to making any investment.

**This report and all information, opinions and conclusions contained in it are protected by copyright. This information may not be reproduced without the prior express written consent of Scotiabank.**

™ Trademark of The Bank of Nova Scotia. Used under license, where applicable.

Scotiabank, together with “Global Banking and Markets”, is a marketing name for the global corporate and investment banking and capital markets businesses of The Bank of Nova Scotia and certain of its affiliates in the countries where they operate, including, Scotiabanc Inc.; Citadel Hill Advisors L.L.C.; The Bank of Nova Scotia Trust Company of New York; Scotiabank Europe plc; Scotiabank (Ireland) Limited; Scotiabank Inverlat S.A., Institución de Banca Múltiple, Scotia Inverlat Casa de Bolsa S.A. de C.V., Scotia Inverlat Derivados S.A. de C.V. – all members of the Scotiabank group and authorized users of the Scotiabank mark. The Bank of Nova Scotia is incorporated in Canada with limited liability and is authorised and regulated by the Office of the Superintendent of Financial Institutions Canada. The Bank of Nova Scotia is authorised by the UK Prudential Regulation Authority and is subject to regulation by the UK Financial Conduct Authority and limited regulation by the UK Prudential Regulation Authority. Details about the extent of The Bank of Nova Scotia's regulation by the UK Prudential Regulation Authority are available from us on request. Scotiabank Europe plc is authorised by the UK Prudential Regulation Authority and regulated by the UK Financial Conduct Authority and the UK Prudential Regulation Authority.

Scotiabank Inverlat, S.A., Scotia Inverlat Casa de Bolsa, S.A. de C.V., and Scotia Derivados, S.A. de C.V., are each authorized and regulated by the Mexican financial authorities.

Not all products and services are offered in all jurisdictions. Services described are available in jurisdictions where permitted by law.