LAURENTIAN BANK SECURITIES

Sébastien Lavoie,
Chief Economist
LavoieS@vmbl.ca
514 350-2931

Dominique Lapointe, CFA,
Senior Economist
LapointeD@vmbl.ca
514 350-2924

April 21, 2021

BC Budget 2021 - Record High Debt Burden Remains Low in the Canadian Context

The good quality of life and sound public finances in British Columbia show that the government has historically took a prudent but effective approach regarding economic policies. Putting people first continues with Finance Minister Selina Robinson delivering her first budget in the midst of a challenging third pandemic wave. New travel restrictions within the province, to be effective later this week, and the lower eligibility age to receive the AstraZeneca vaccine will contribute to taper off the new infection curve.

Important downward revision to last year's deficit

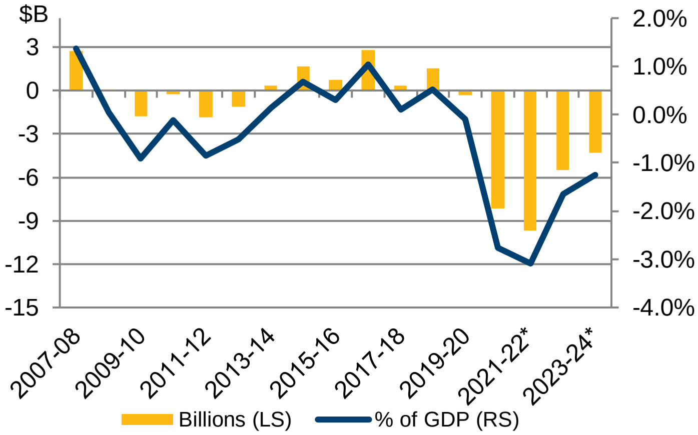
Before discussing the 3-year fiscal outlook, it is worth highlighting the important fiscal improvement in the third quarter of FY 2020-21. The deficit estimate is revised down to $8.1B (2.8% of GDP), significantly lower than the $13.6B shortfall projected in the Fall 2020 Update. The main drivers of this sizzling $5.1B improvement are taxation revenues, up $2.3B. Higher corporate income taxes and provincial sales taxes lead the way. Federal transfers were also $0.6B more generous than projected. Lower-than-expected operating expenses, including at the crown corporation ICBC, and higher lumber prices generating additional royalties contributed to the improvement as well. In summary, the 3-year fiscal outlook proposed in this budget begins on a better footing than we were expecting.

The economic outlook has improved since the Fall 2020 Update, both at the global and domestic levels. As of March, the level of employment was back to pre-COVID levels in British Columbia, an impressive development. Budget 2021 assumes a return to pre-pandemic real GDP levels by 2022. Total revenues are projected to decline by $1B, to $58.9B in FY 2021-22 as the moderate improvement in taxation and non-renewable resource revenues is not expected to fully compensate for the pullback in federal transfers and crown corporation revenues. Revenues soar in the second and third years of the 3-year fiscal plan, by an average annual rate of 5.1%.

Record deficit in FY 2021-22

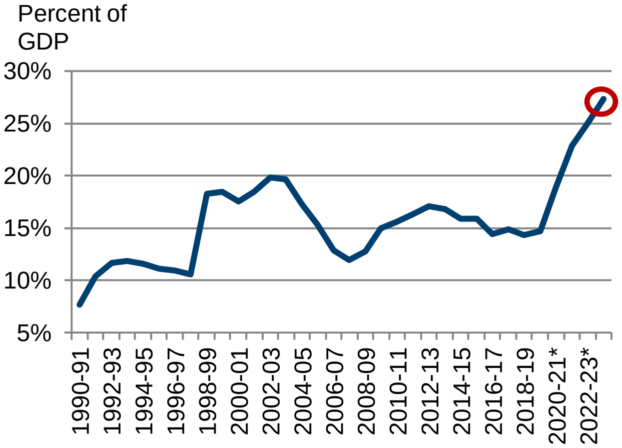
The deficit increases to $9.7B in FY 2021-22 (3.1%), the steepest on record, due to a temporary boost in spending associated to the Province's health and financial support to people and businesses. Total expenses are poised to grow 4.5%, to $64.4B. Deficits decline in the second and third year of the outlook: to $5.5B (1.7% of GDP) and $4.3B (1.3% of GDP), respectively. In comparison, deficits-to-GDP ratios registered during and after the 2008-09 financial crisis stood at less than 1% (chart 1)

Chart 1: BC Budgetary Balance



Source: Government of British Columbia, LBS Econ. Res. and Strategy.

Chart 2: BC Net Debt



Source: Government of British Columbia, LBS Econ. Res. and Strategy.

Pandemic-uncertainty led the government to build in several layers of prudence in the fiscal framework. Various contingencies and forecast allowance add up to $4.3B in FY 2021-22, $1.8B in FY 2022-23 and $0.7B in FY 2023-24. The $4.3B buffer is particularly large, representing 7% of revenues. Unused in an optimistic scenario where the pandemic ends sooner-than-expected, the FY 2021-22 deficit could be cut by almost half.

No detailed plan to return to balance

Beyond FY 2023-24, like many provinces this budget season, the government falls short of providing investors a precise path to balance. It nonetheless specifies that "*preliminary analysis indicates a return to balanced budgets within a range of seven to nine years (the period of 2028/29 - 2030/31*)". A specific timeline will be provided in Budget 2022.

Debt remains low compared to other jurisdictions

The Province's public debt burden remains low compared to other subnational jurisdictions. It is somewhat less appealing compared to its own past. The taxpayer debt-to-GDP ratio, which has historically trended at low levels, will move above 20% for the first time in history. Net debt-to-GDP will follow a similar path, reaching 27% in FY 2023-24 (chart 2). The debt-to-revenue ratio, close to 85% pre-COVID, will increase from 103% in FY 2020-21 to 148% in FY 2023-24. Servicing the debt will remain affordable despite costing a little more down the road as interest rates are projected to increase. The cents per dollar of revenue dedicated to debt servicing will remain below 4 cents, lower than other jurisdictions and lower than in previous decades when interest rates were higher.

Finally, this year's record $19.2B bond issuance program is being driven by operational deficits and high capital requirements ($13.5B). Infrastructure projects underpin BC's recovery plan, including the Broadway transit line, the construction of new hospitals and the addition of affordable rental homes. In FY 2022-23 and FY 2023-24, borrowing requirements are projected to slightly edge down, to $17.8B and $15.0B, respectively. Of note, we expect internal financing sources to reduce borrowing needs in every of those years (those adjustments amounted to $3.5B in FY 2020-21).

Sébastien Lavoie | Chief Economist
514 350-2931 | lavoies@vmbl.ca