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Sustained deficits (and accumulating debt) in pivot to tariff defence

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Highlights

As fiscal year 2024-25 draws to a close, British Columbia is on track to run a $9.1 billion budgetary shortfall (2.1% of GDP). That's technically a bit lighter than what was outlined in the mid-year update but is still well above the $7.9 billion deficit anticipated in Budget 2024. Looking ahead, an uncertain economic outlook clouded by trade-related noise will see the province's deficit grow to $10.9 billion (2.5% of GDP) in 2025-26. There's technically some consolidation in the subsequent years but both 2026-27 and 2027-28 are expected to register deficits >2% of GDP ($10.2 billion and $9.9 billion, respectively). As other Canadian provinces have highlighted, B.C. concedes there's a high degree of uncertainty on Canada-US trade relations. While the fiscal plan's base case projection does not involve sweeping U.S. tariffs and Canadian retaliation, associated uncertainty still weighs on the outlook. Consistent with the large(r) deficits, a list of new provincial initiatives aims to defend the B.C. economy against U.S. tariffs. The province provides $9.9 billion in new operating spending over the course of the plan focused on health care, education and social services. Given the path for the budget, it follows that the province's debt curve is pointed higher. Indeed, its debt burden is set to grow in both nominal and relative terms, as the three -year plan envisions $69 billion in new taxpayer-supported being added. Debt servicing costs currently consume just 4.3% of revenue but that's set to grow, nearing 7% by 2027-28. British Columbia's gross borrowing requirement, which amounted to $29.2 billion in the outgoing fiscal year, is also about to increase. The province pencils in $31.1 billion of debt issuance for 2025-26, with growth expected in subsequent years (reaching $34.7 billion in 2027-28).

- **Economic outlook** — Impacted by interest rates that were still restrictive, it is estimated that the real GDP of B.C. grew moderately by 1.2% in 2024, which is less than the 1.5% observed in the country as a whole. More important for public finances, nominal GDP grew by 4.1% (Canada: 4.6%). Given that BC households are among the most indebted in the country, financial easing caused by interest rate cuts was expected to lead to more robust growth in 2025 and beyond, but the trade war that began this week with the United States is clouding the province's budget plan. Indeed, the economic outlook on which the budgetary framework is based does not include the introduction of tariffs by the Americans or retaliatory measures by Canada. However, the budget exercise nevertheless takes the opportunity to present the impact of a tariff war on a certain economic variable. In its baseline scenario (which excludes tariffs), the budget forecasted a growth of 1.8% in real GDP in 2025, followed by increases of 1.9% in 2026 and 2027, which is in line with the average of private sector forecasters. Real GDP is then expected to increase by 2.1% in 2028 and 2.2% in 2029. As for nominal GDP, growth of 4.3% has been forecast for 2025 and 2026, followed by 4.2% in 2027, 4.4% in 2028 and 4.5% in 2029. Still according to the reference scenario, the average annual unemployment rate is expected to rise from 5.6% in 2024 before reaching a peak of 5.7% in 2025, then gradually decrease from 5.4% in 2026 to 5.0% in 2029.

  In the case of a tariff war, where the US imposes tariffs of 25% on all Canadian goods, except for a 10% tariff on energy and which includes retaliatory measures on the part of Canada, the economic scenario is obviously much more pessimistic. Indeed, real GDP growth is expected to be only 0.3% in 2025 and 0.8% in 2026 (compared to 1.8% and 1.9% respectively). This scenario would result in a real GDP that is $9.6 billion lower than in the baseline scenario in 2029, representing a cumulative loss of $43 billion over this horizon. The budget does not detail the impact of tariffs on nominal GDP, which has a greater impact on public finances than real GDP. As for the labor market, it is anticipated that 45,000 fewer jobs than previously predicted will be created by 2029. As a result, the unemployment rate is expected to rise to 6.4% in 2025 and 6.7% in 2026 (compared to 5.7% and 5.4%, respectively).

- **Outgoing year budget balance (2024-25)** — Not unlike other provinces, British Columbia's budget balance has been under pressure since this time last year, as is evident in updated guidance for the outgoing 2024-25 fiscal year. The $7.9 billion deficit projected in Budget 2024 was revised to $9.1 billion (2.1% of GDP) today. Note however, revised thinking on this outgoing fiscal year is $273 million *better* than the second quarter update as higher corporate revenue and crown corporation income more than offset statutory compensation spending and shelter-related costs.

- **Medium-term fiscal outlook (2025-26 & beyond)** – British Columbia is set to extend its streak of deficits to three years in 2025-26, as the province is guiding towards a $10.9 billion shortfall (2.5% of GDP, 13.0% of revenue). For context, the latest official thinking on the 2025-26 budget balance came in a September update where a $6.7 billion deficit was pencilled in. The source of budgetary pressure is spending growth (+3.2%), led primarily by health care, outpacing revenue growth (+1.4%). Tepid revenue growth is primarily a function of a large decline in corporate tax inflows (-$2.1 billion, or -25%), although this drop-off is a due to abnormally high 2024-25 receipts and was flagged back in Budget 2024.

  Further out the forecast horizon, deficits will be reined in a touch but only marginally. A $10.2 billion shortfall (2.3% of GDP, 11.9% of revenue) has been pencilled in for 2026-27 and a $9.9 billion deficit (2.2% of GDP, 11.2% of revenue) is expected in 2027-28. The modest consolidation in these outer years is expected to be a function of revenue growth (+2.4%) outpacing better-contained expense growth (+1.6%). For additional context, the combined deficit over the three overlapping years of Budget 2024 and Budget 2025 (i.e., 2024-25 to 2026-27) moves from $22.0 billion in last year's budget to $30.3 billion in this year's.

  As far as prudence is concerned, the province's fiscal plan does not include the provision of a forecast allowance but does include Contingencies Vote estimates of $4 billion in each year of the fiscal plan. These reflect "funding set aside for uncertain or unforeseen matters, future initiatives, caseload pressures, and new collective bargaining mandate costs". When it comes to planning assumptions, implementation of U.S. tariffs and Canada's response are not *explicitly* incorporated in the budget, however, uncertainty is reflected in growth forecasts. In addition, the province provides a tariff scenario that estimates up to $1.4 billion in revenue pressures if broad tariffs were levied and sustained. British Columbia also offers its regular course fiscal sensitivities, which suggests 1%-pt of additional nominal GDP growth is worth $200-300 million.

- **New initiatives** - Dubbed 'Standing Strong for B.C.', Budget 2025 highlights the economic headwinds stemming from trade and geopolitical uncertainty and includes four major lines of action, titled: "strengthening health care and services people rely on", "a strong, diversified economy for B.C.", "B.C. lowering costs, providing affordable homes", and "making communities stronger, safer". On the services front, Budget 2025 will invest $7.7 billion over the next three years to support healthcare, education, and social services. This is comprised of $4.2 billion aimed at increasing healthcare system capacity, allocating $870 million to the support the opening and operation of new facilities, and $443 million to support the primary care strategy. $500 million in new funding over three years will contribute to improvements in addiction recovery and treatment programs. In K-12 education, $370 million will be devoted to increasing teaching staff and supporting youth with special education needs. Relating to diversifying B.C.'s economy, the province outlines $172 million in new investments, intended to grow a more independent and risk-prudent economy. Leveraging existing industry strengths, B.C. will boost tax credits in the production industry – the Interactive digital media credit will be made permanent, and will increase from 17.5% to 25%, while the film incentive credit (for Canadian productions) will increase from 35% to 40% (international productions services tax will increase from 28% to 36%). In addition, Budget 2025 includes $142 million for highways and transit maintenance. In attempting to improve housing affordability, Budget 2025 presents $318 million in additional funding for BC home building. Speculation and vacancy taxes will also increase for both foreign and Canadian owners beginning in 2026 and will generate an estimated $47 million in revenues in the 2027-28 fiscal year. In support of low-income families, B.C. will raise the income threshold for the Rental Assistance Program from $40,000 to $60,000, nearly doubling the number of families that will be eligible. The average supplement these families receive will also increase 75% to $700 per month. In a similar initiative, more seniors will benefit from the Elderly Renters program, as income thresholds and payments (+30%) will increase too. Lastly on the cost-of-living front, the province will provide a one-time ICBC relief rebate of $110 to approximately 3.7 million ratepayers, expecting a return of $410 million to policyholders. In the final portion of Budget 2025 initiatives, B.C. outlines $325 million in new funding over three years aimed at providing community housing improvements. The province will also allocate $90 million in additional funding to expand the HEART and HEARTH homelessness-alleviation programs into new communities. Finally, $67 million will be committed to improving community safety programs, and $104 million in additional funding will go towards policing programs, expanding training capacity from 192 to 288 officers each year.

- **Debt outlook & interest bite** British Columbia's preferred debt measure—taxpayer-supported debt—is poised to end the outgoing 2024-25 fiscal year at $97.7 billion. That's some $9 billion higher than the original 2024 budget target, reflecting an upwardly revised base, a larger-than-planned 2024-25 deficit (vs. budget) and early pre-funding (towards 2025-26). Some $22 billion in net new taxpayer-supported debt was taken on in 2024-25 and forecasted budget deficits, along with planned capital outlays, will keep BC's debt curve pointed higher. The budget envisions roughly $69 billion in new taxpayer-supported being added over the coming three fiscal years (the debt level forecast at $166.5 billion by 2027-28). Controlling for underlying growth in the economy, BC's taxpayer-supported debt burden is also stepping up. Pre-COVID, taxpayer-supported debt hovered around 15% of GDP but is now estimated to end 2024-25 at 22.9%. That closely watched ratio is anticipated to rise to 26.7% in 2025-26, ultimately reaching 34.4% by 2027-28. Overall, this is a relatively rapid pace of debt accumulation that partially erodes BC's once-sizeable balance sheet edge vs. the weighted provincial average. Under the banner of "fiscal sustainability", the budget notes that BC is striving to "flatten growth in the Province's Debt-to-GDP ratio in the near term, with the longer term goal of declining Debt-to-GDP once balanced operating results are achieved." The budget goes on to note that the eventual path to balance (and thus debt containment) will "require careful management of provincial spending", with the government committing to various expenditure management initiatives.

  Reflecting BC's historically low debt burden, the taxpayer-supported interest bite remains relatively modest/limited. For the outgoing 2024-25 fiscal year, related interest costs are expected to consume just 4.3% of total provincial revenue. That continues to compare favourably to the weighted provincial average. In light of planned debt accumulation, a larger interest bite has been telegraphed going forward, the taxpayer-supported debt affordability measure estimated at 4.9% of revenue for 2025-26 and nearing 7% by 2027-28.

  For planning purposes, the yield on 10-year Canada bonds is seen averaging 3.08% in calendar 2025 vs. 3.34% actual for 2024, although such financial market assumptions (like the overall geopolitical and economic outlook) remain highly uncertain. Fiscal sensitivity analysis suggests that a 1%-pt surprise in interest rates equates to a $220 million annual fiscal impact.

- **Borrowing requirement** — British Columbia's gross borrowing requirement amounted to $29.2 billion in 2024-25 vs. an original plan of $24.2 billion. Among other things, that $5 billion increase reflected a larger budget deficit (vs. budget) alongside the decision to pre-finance a portion of the coming year's funding need. Reflecting on the outgoing year's borrowing program, BC secured $26.8 billion from term markets, with nearly two-thirds of the province's bond supply steered to international markets. A further $2.2 billion was raised via increased short-term borrowing. Officially, there is no borrowing remaining to be done between now and fiscal year end. Notwithstanding pre-borrowing efforts, BC's increased budget deficit, enhanced capital requirements and larger maturities add up to a gross borrowing requirement of $31.1 billion for 2025-26. That's a relatively sizeable borrowing requirement by BC standards, but as was aptly demonstrated in the outgoing fiscal year, expect BC to "continue to look to both domestic and international markets to address funding requirements, and continue to expand its investor base." While heightened economic and geopolitical uncertainty could ultimately alter the fiscal trajectory (not just in BC but all across Canada), the budget projects even larger gross borrowing requirements further out: $33.1 billion for 2026-27 and $34.7 billion for 2027-28.

- **Current long-term credit ratings** — S&P: AA-, Negative | Moody's: Aaa, Negative | DBRS: AA(H), Stable
  [Refer to our Provincial Ratings Snapshot for additional colour on specific credit rating drivers/considerations]

British Columbia

$000,000	Budget 2024/25	Forecast 2024/25	Budget 2025/26	Plan 2026/27	Plan 2027/28
Taxation revenue	49,214	49,532	49,699	51,418	54,189
Resource revenue	3,150	2,334	2,997	3,334	3,249
Other revenue	11,400	12,318	12,019	12,116	12,147
Other federal transfers	14,446	14,189	15,277	14,889	14,576
Commercial Crown corporation net income	3,313	4,495	4,011	3,958	4,004
as of Insurance Corporation of British Columbia (ICBC)	-	*1,400*	*800*	*700*	*700*
Total revenue	**81,523**	**82,868**	**84,003**	**85,715**	**88,165**
Program spending	81,444	83,745	85,855	85,969	86,874
Debt servicing costs	4,105	4,373	5,060	5,949	7,154
Contingencies	3,885	3,885	4,000	4,000	4,000
Total spending	**89,434**	**92,003**	**94,915**	**95,918**	**98,028**
Surplus/Deficit	**(7,911)**	**(9,135)**	**(10,912)**	**(10,203)**	**(9,863)**
Provincial Debt Changes					
Deficit (surplus) before forecast allowance	7,911	9,135	10,912	10,203	9,863
Taxpayer-supported capital spending	14,104	11,348	15,374	15,754	14,735
Self-supported capital investments	4,652	4,622	4,828	4,628	4,592
Commercial Crown corp. retained earnings	751	1,972	1,545	1,450	1,440
Amortization and other capital asset changes	3,170	3,142	3,336	3,490	3,692
Other items	(11,104)	(30,219)	(12,379)	(8,445)	(9,204)
Increase in total provincial debt	**19,484**		**23,616**	**27,080**	**25,118**
Total provincial debt	**123,267**	**133,016**	**156,632**	**183,712**	**208,830**
Taxpayer-supported	**88,639**	**97,711**	**118,719**	**143,412**	**166,479**
Self-supported	**34,628**	**35,305**	**37,913**	**40,300**	**42,351**
Total provincial debt / GDP	29.2%	31.2%	35.2%	39.6%	43.2%
Taxpayer-supported	21.0%	22.9%	26.7%	30.9%	34.4%
Capital Spending	**18,756**	**15,970**	**20,202**	**20,382**	**19,327**
Taxpayer-supported capital spending	14,104	11,348	15,374	15,754	14,735
Self-supported	4,652	4,622	4,828	4,628	4,592
Provincial borrowing requirements	**24,406**	**29,453**	**31,877**	**33,450**	**34,852**
Operating deficit (surplus)	7,911	9,135	10,912	10,203	9,863
Capital spending	18,756	15,970	20,202	20,382	19,327
Refinancing requirements	3,670	3,806	8,155	6,282	8,843
Other financing sources	(5,931)	542	(7,392)	(3,417)	(3,181)

Source: Budget documents, British Columbia Ministry of Finance

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