Canadian Provinces

Credit Update And Fiscal Outlook

S&P Global Ratings

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October 2023

This report does not constitute a rating action

Canada Macro Forecast Q4 2023

Challenges Ahead

- S&P Global Ratings expects the Canadian economy to have subpar GDP growth this year and in 2024.
- What started as a mild contraction in the second quarter--as strikes and wildfires hindered activity--is just the beginning of a drawn-out sluggish growth path for the next several quarters as the economy begins to feel the impact of high interest rates.
- The Bank of Canada's monetary tightening stance is poised to continue in the near term. We have penciled in one more rate hike in the fourth quarter and the first 2024 rate cut, likely in the second quarter.

S&P Global Ratings' Canada economic forecast overview
September 2023 (annual average % change)

Key indicator	2019	2020	2021	2022	2023f	2024f	2025f	2026f
Real GDP	1.9	-5.1	5.0	3.4	1.2	1.2	1.5	1.8
Change from June (percentage point)					-0.3	0.0	-0.2	-0.1
Domestic demand	1.1	-5.6	6.9	4.9	-0.7	0.4	1.5	1.5
Consumer spending	1.5	-6.1	5.0	4.8	2.0	1.0	1.9	1.8
Nonresidential fixed investment	3.1	-9.4	4.5	4.6	1.3	1.2	1.4	1.4
Residential investment	-0.7	5	14.9	-11.2	-12.8	-0.9	1.0	1.8
Government consumption	1.0	1.3	6.4	2.0	0.2	-0.7	-0.2	1.4
Real exports	2.7	-8.8	1.5	2.9	5	2.8	2.4	2.2
Real imports	0.4	-9.1	8.0	7.5	-1.3	0.5	2.1	1.5
CPI	2.0	0.7	3.4	6.8	3.9	2.2	2.5	2.1
Core CPI	1.8	1.2	2.9	5.6	3.7	2.4	2.1	1.9

Note: All percentages are annual averages, unless otherwise noted. Core CPI is consumer price index excluding energy and food components. f--Forecast. Sources: StatCan, Bank of Canada, S&P Global Market Intelligence Economic Simulink, S&P Global Ratings Economics' forecasts.

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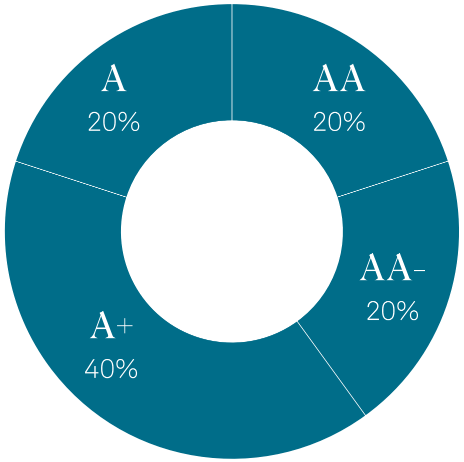
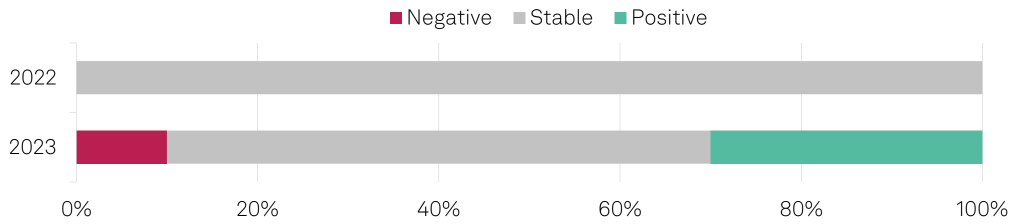
Rating Trends: Canadian Provinces

Mostly positive movement in credit ratings this year as fiscal performance diverges

Rating and outlook distribution

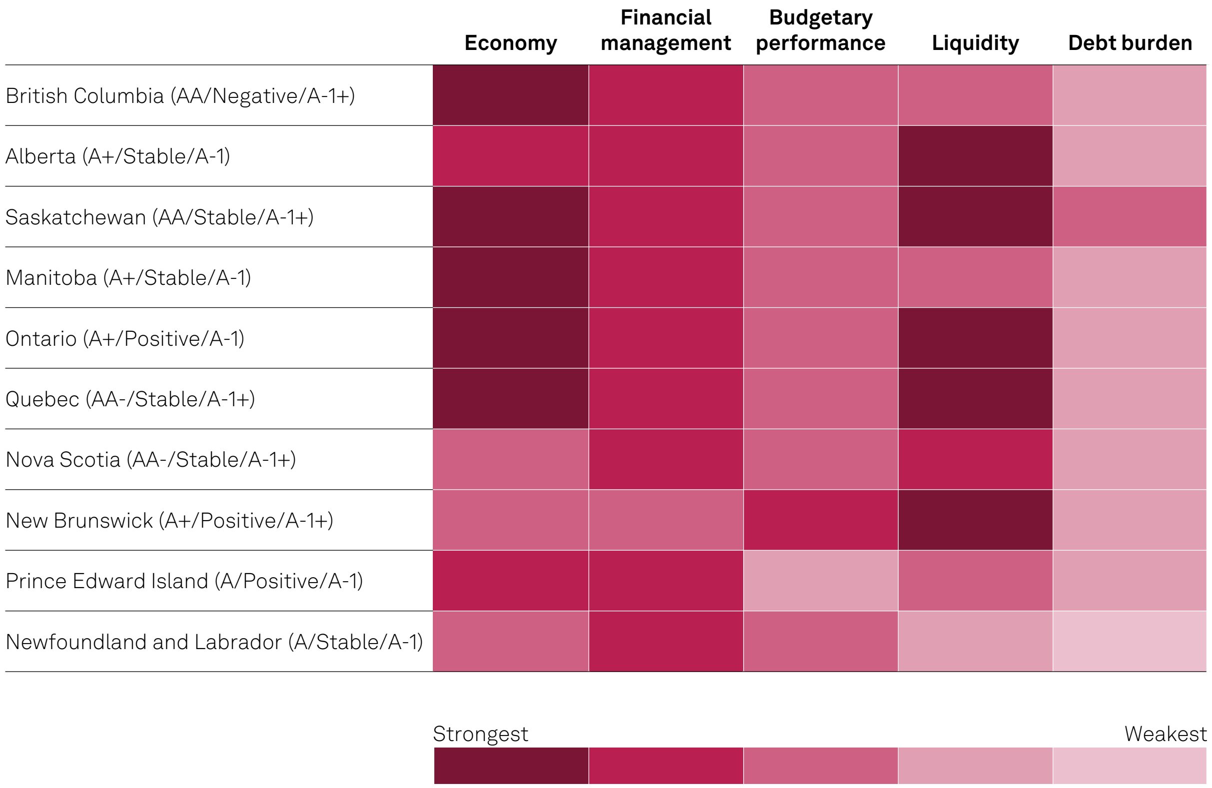
October 2023





Source: S&P Global Ratings.

Ratings and key assessment factors



Credit And Rating Trends: Ongoing Risks For Provinces

Wage Pressure: Provincial revenue growth has outpaced expenditures for the past three years, yet persistent inflation and labor market tightness are putting upward pressure on wages. That will hit budgets at different times depending on wage-contract structures and terms.

Higher-for-Longer Rates: Longer amortization at fixed rates partially insulates provincial budgets from recent interest rate movements, but the longer rates stay high, the more they will begin to bite for those with high borrowing needs and faster rollovers.

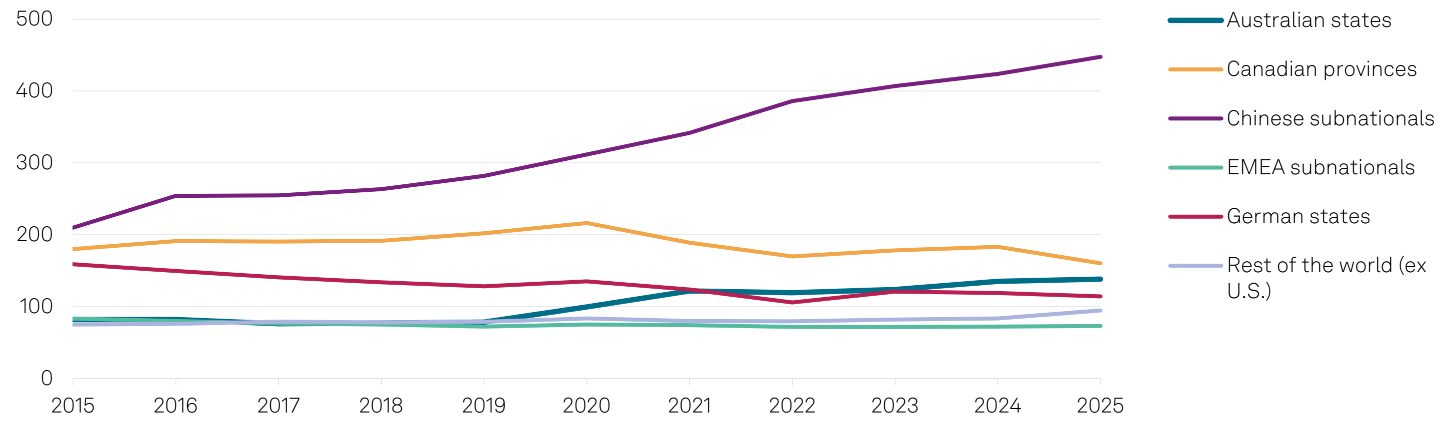
Infrastructure and Climate Adaptation: Provinces' long-term plans for climate adaptation, mitigation, and transition will increase in importance as climate-related events become more frequent and severe. Disaster recovery arrangements, such as Canada's Disaster Financial Assistance Arrangements, will need to evolve to balance long-term financial sustainability and risk-sharing. This could increase the cost to recover from disasters and affect long-term investment and borrowing needs.

Population Growth: Canada’s recent population growth boosts tax revenue and consumer spending during a period of slower economic growth; it also adds to affordability challenges in urban areas, and will increase demand for public services, including health care services, which make up a large share of provincial budgets.

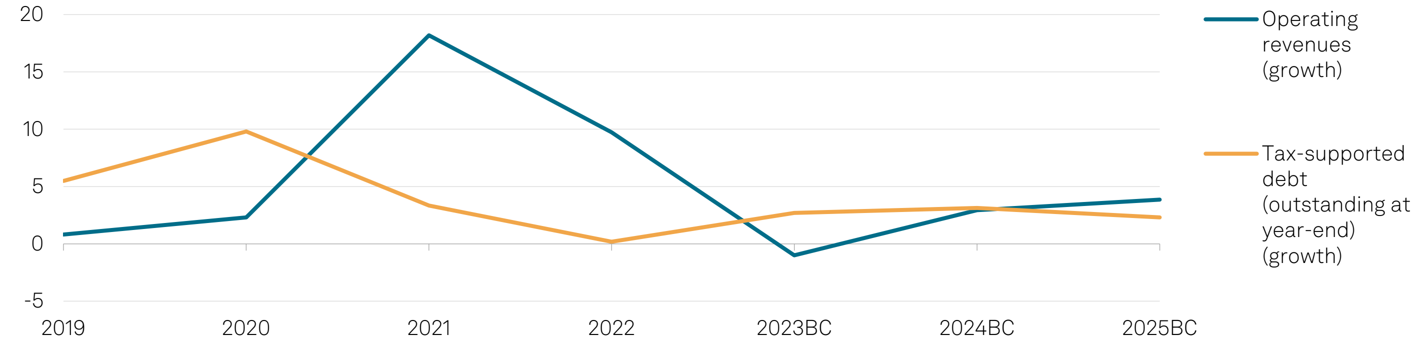
Provinces' Debt Burden Will Moderate, But Remain High By Global Standards

- Debt as a share of revenue will inch back up from 2022 levels but remain below even 2019 levels.
- Rapid revenue growth and debt retirement in the two years post-pandemic left provincial debt burden at its lowest level in a decade in 2022.
- Nevertheless, Canadian provincial debt levels are high by global standards.

Tax-supported debt (% consolidated op. rev.)



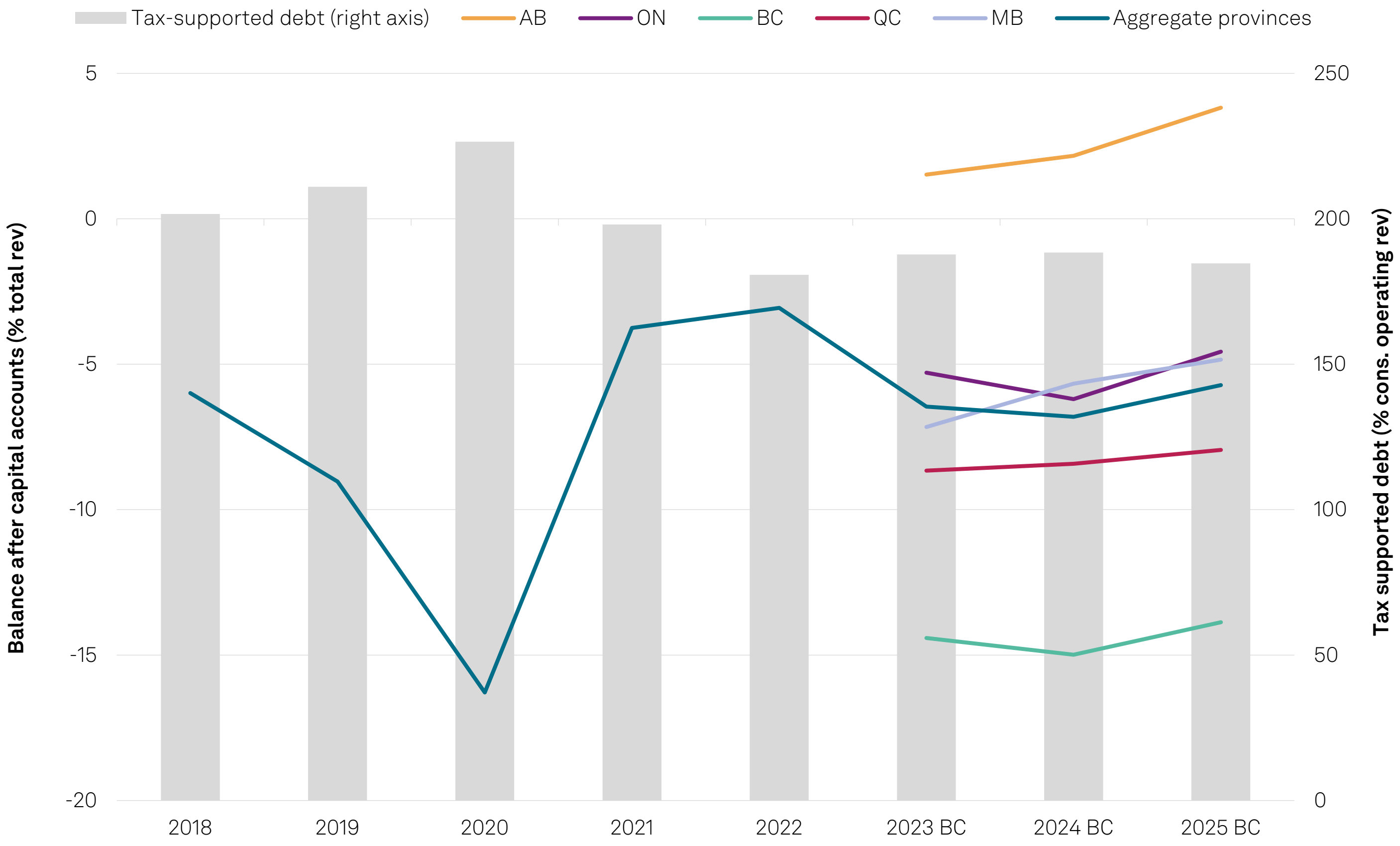
As revenue growth slows, debt ratios will stabilize (annual % change)



BC—Base case. Source: S&P Global Ratings

Provinces' fiscal performance will diverge as debt burdens ease

As revenue growth slows, the path to structural balance will take budget discipline



BC—Base case. Source: S&P Global Ratings

- Inflation has boosted provinces' revenue beyond expectations for the last two fiscal years, while expenditures (particularly in personnel) have been slower to catch up
- We expect fiscal results to moderate for most provinces starting in 2024 as revenue growth slows and wage contracts adjust
- Excepting commodity-producing provinces, the path to budget balance for most will take longer than previously expected

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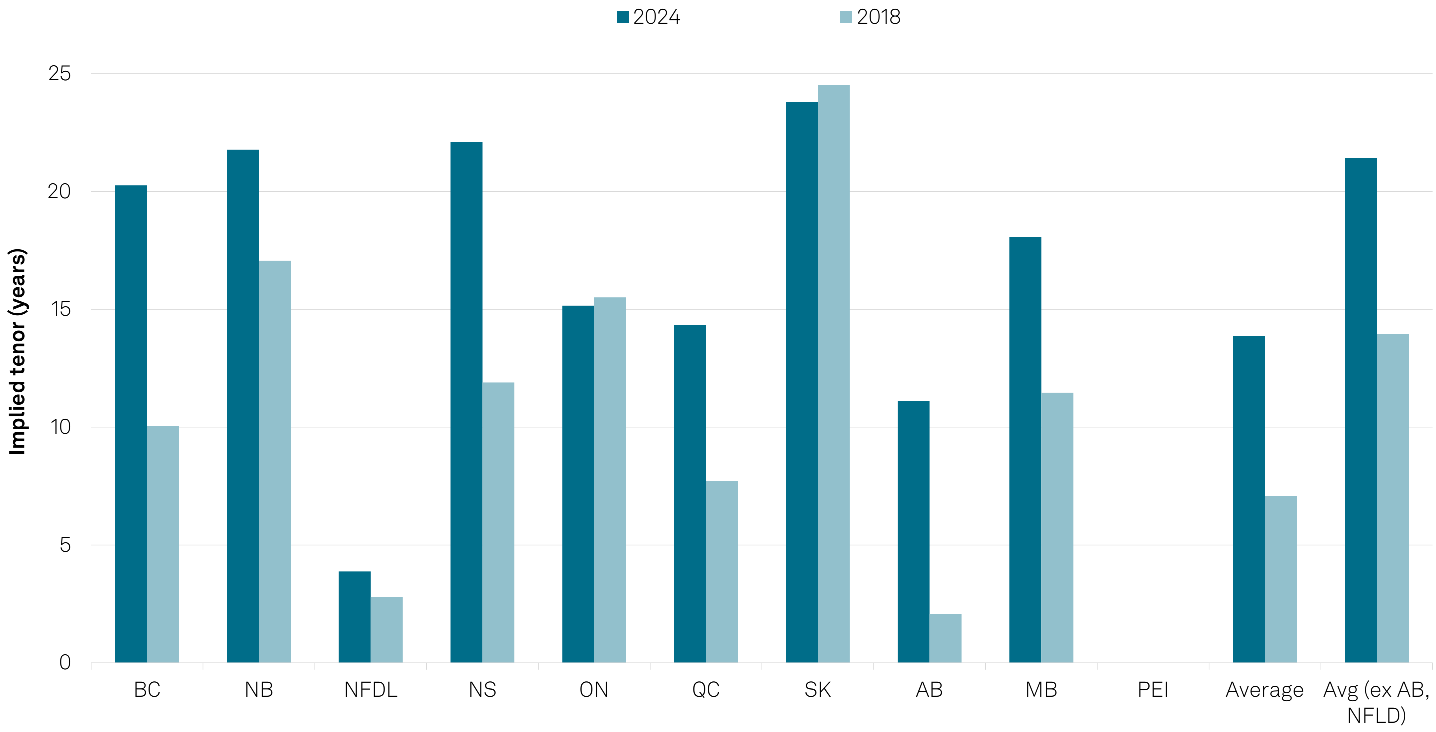
Longer amortization takes some of the bite out of higher-for-longer

Interest costs will remain manageable over the next two years

Implied tenor of debt

Based on annual principal repayment % outstanding principal at year-end



Source: S&P Global Ratings

- Slower average amortization of provinces' debt will take some of the bite out of higher interest costs, although debt servicing expense continues to grow
- We project the average implied tenor of provinces' debt to be 17 years in 2024 versus 11 years in 2018
- Average interest costs will remain manageable, rising to 6.5% of operating revenue in 2025 from 5.7% in 2022

Fiscal And Debt Forecasts

Fiscal 2023-2024 Expectations: Base Case

Provinces started the year on strong footing, but will need to prepare for economic slowdown

Base Case

- Most provinces are focused on fiscal consolidation
- Pace of debt growth will pick up modestly this year following a post-pandemic dip
- Lower debt service requirements and better after-capital outcomes result in stronger liquidity metrics
- Rising interest rates will have a modest impact in the short term, given low proportion of variable-rate debt and longer bond terms
- Resource-rich provinces have benefitted from high commodity prices

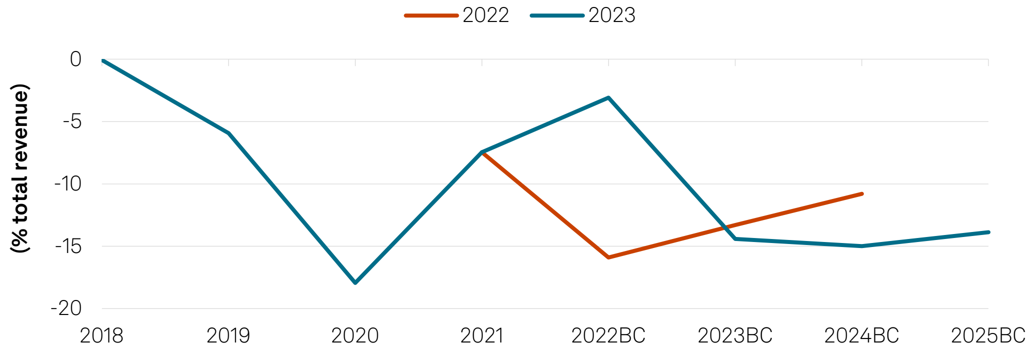
Downside Risks

- Economic headwinds could stifle fiscal 2024 budgetary outcomes
- Large capital programs, in part, will offset current gains for some
- The impact of collective agreement renewals on budgetary performance could be larger than expected
- Prior-year adjustments could bring volatility in fiscal outcomes.
- Election results in Manitoba and a potential early election in New Brunswick will bring some uncertainty to fiscal trajectories.

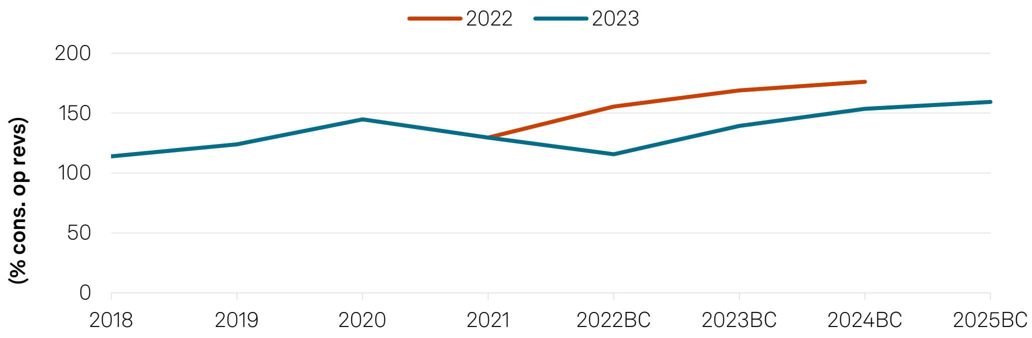
British Columbia

AA/Negative/A-1+

British Columbia balance after capital accounts



British Columbia tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- The 2023 budget outlines an extensive investment plan for operations and record levels of capital spending, which will reverse the fiscal gains made in the past two years.
- Large spending plan on health care and infrastructure along with higher operating expenses commitment will lead to the return of sizable after-capital deficits.
- As a result, B.C.'s debt will steeply rise and will remain high compared with that of peers.

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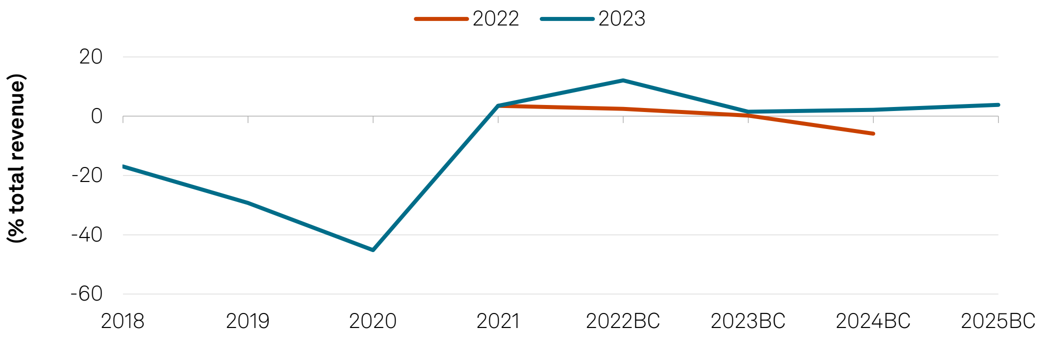
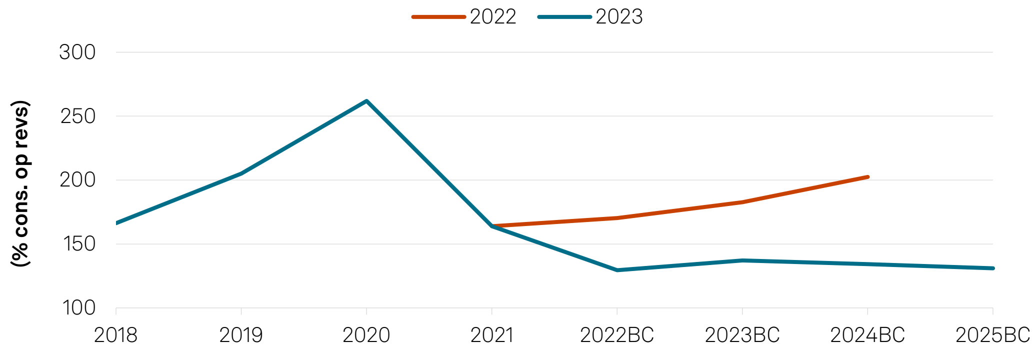
Alberta

A+/Stable/A-1

Alberta balance after capital accounts



Alberta tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- Continuing high West Texas Intermediate prices along with high tax revenues keep operating and after-capital surpluses at levels not seen in a decade.
- Alberta's debt burden will decline notably as the province repays maturities and liquidity will remain robust.
- Fiscal policies are important as the province's economy and fiscal results are significantly influenced by swings in oil prices, making its budgetary performance more volatile than that of peers.

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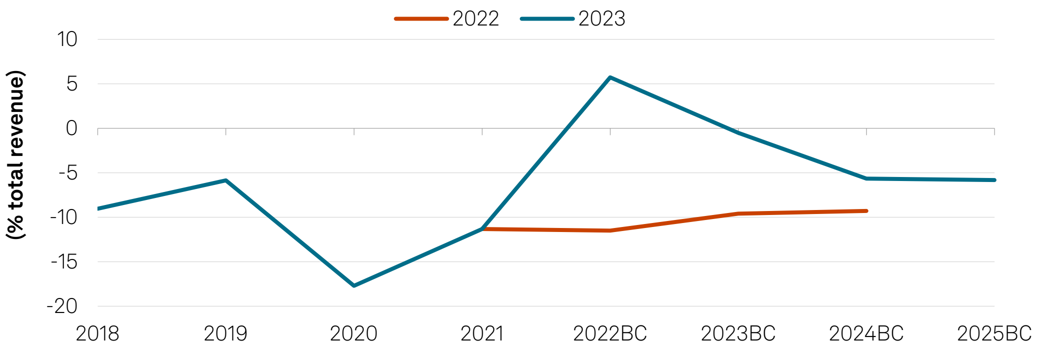
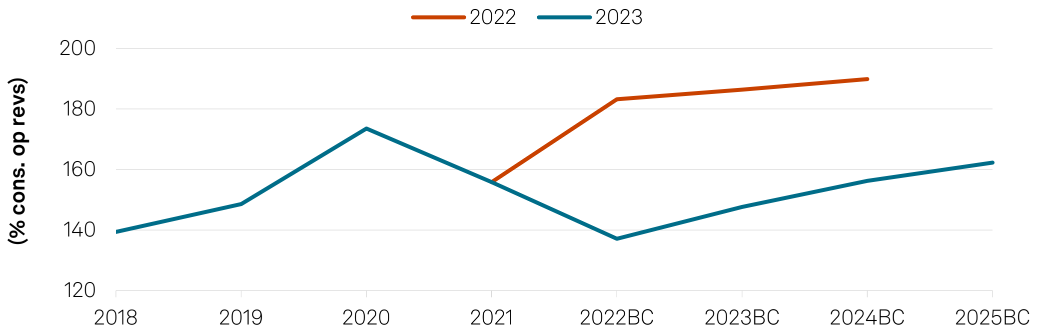
Saskatchewan

AA/Stable/A-1+

Saskatchewan balance after capital accounts



Saskatchewan tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- Economic growth will slow down with the decline in commodity prices in 2023 (fiscal 2024) and translate into lower non-renewable resource revenue.
- Fiscal balance is achievable over the medium term although inflationary pressure and lower commodity prices could limit surpluses.
- Saskatchewan to retire about C$1 billion of operating debt in 2024, but elevated capital expenditures will lead to a net increase in borrowing in the next few years.

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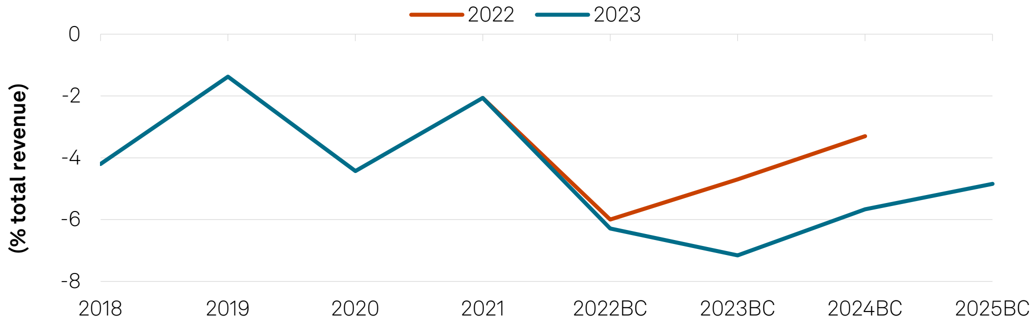
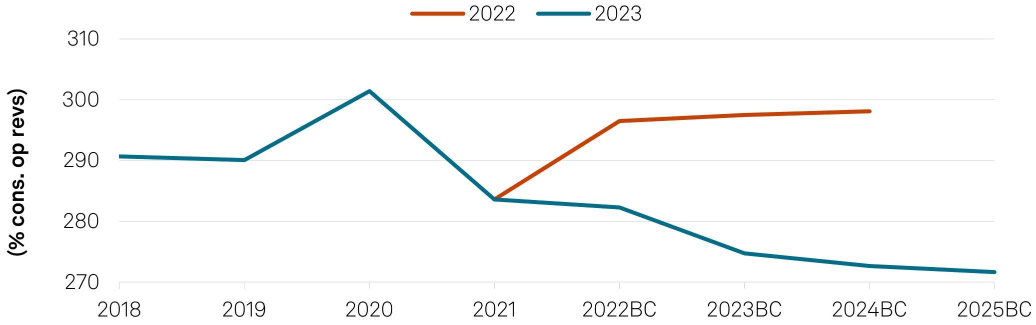
Manitoba

A+/Stable/A-1

Manitoba after capital balance



Manitoba tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- 2023 budget prioritized tax cuts during an election year, which leads to weaker fiscal results compared with the previous forecast.
- After-capital deficits will gradually decline over the outlook horizon, but the path to fiscal balance will take longer than previously expected.
- Debt as a share of revenue will fall marginally in the medium term.
- The recent election might bring further uncertainty regarding fiscal policy.

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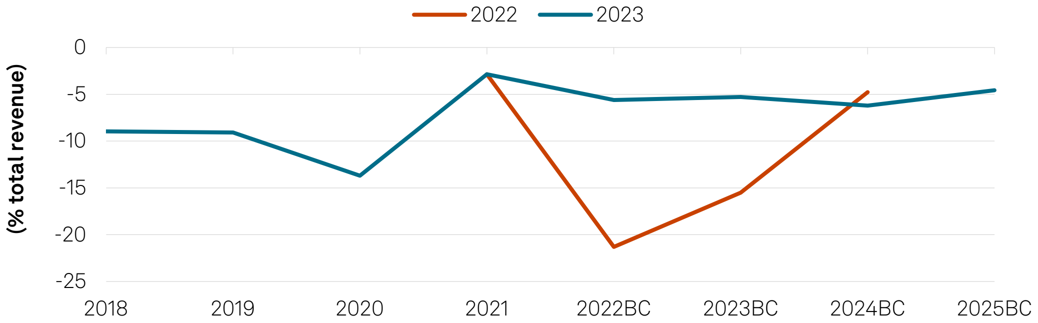
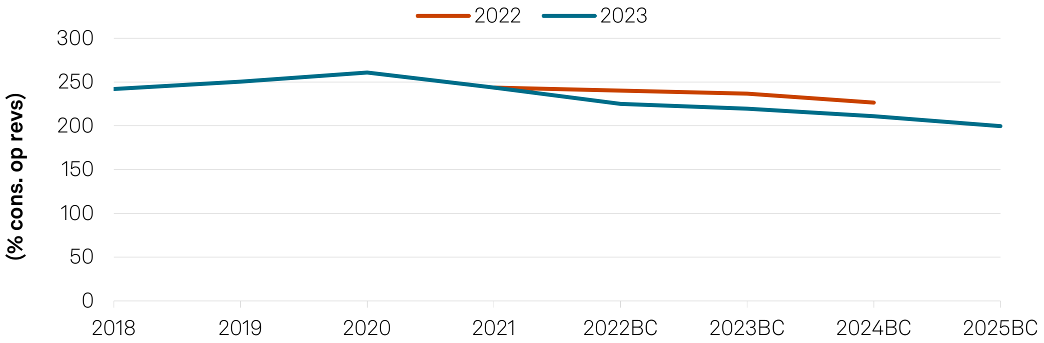
Ontario

A+/Positive/A-1

Ontario balance after capital accounts



Ontario tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- Despite weaker-than-expected fiscal 2023 results, we expect the province will continue with its fiscal consolidation efforts, despite near-term economic headwinds.
- An ambitious capital program aimed at improving transportation networks and investing in the health care system, in advance of population growth, will lead to funding gaps that will necessitate borrowing and result in a moderate rise in the province's debt.
- Nevertheless, a focus on debt stabilization will continue.

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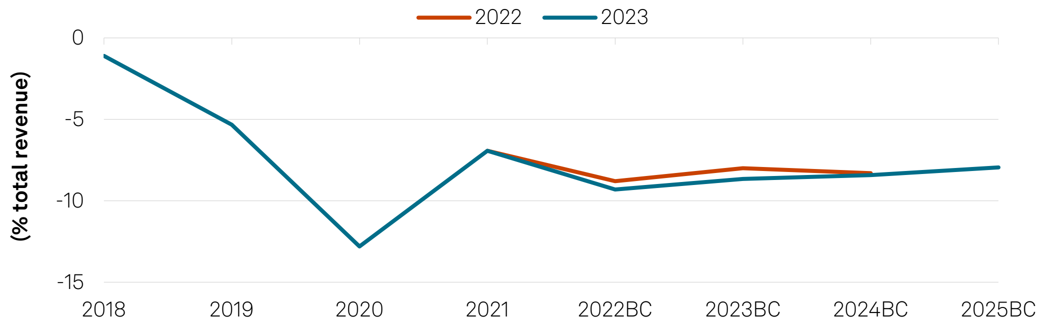
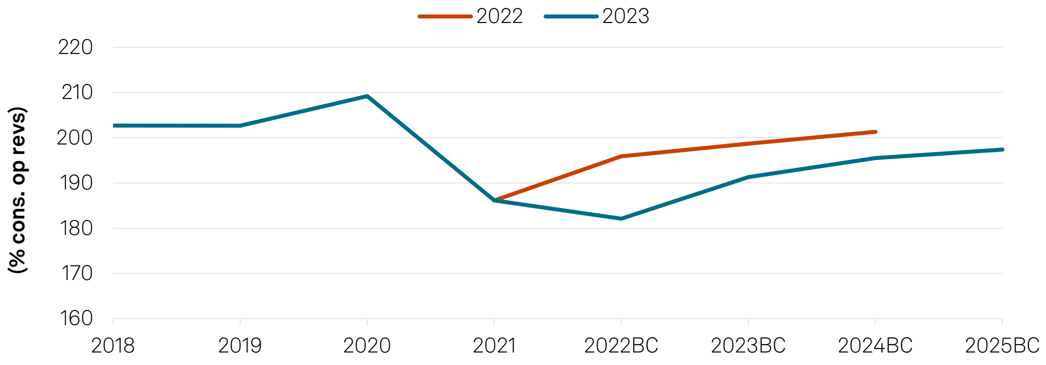
Quebec

AA-/Stable/A-1+

Quebec balance after capital accounts



Quebec tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- Despite near-term economic headwinds, we expect that a prudent fiscal framework will result, on average, in modest operating surpluses and moderate after-capital deficits.
- The province is implementing tax measures to stimulate the economy and investing in key priorities such as health care and infrastructure.
- The debt trajectory will remain relatively stable in the next two years.

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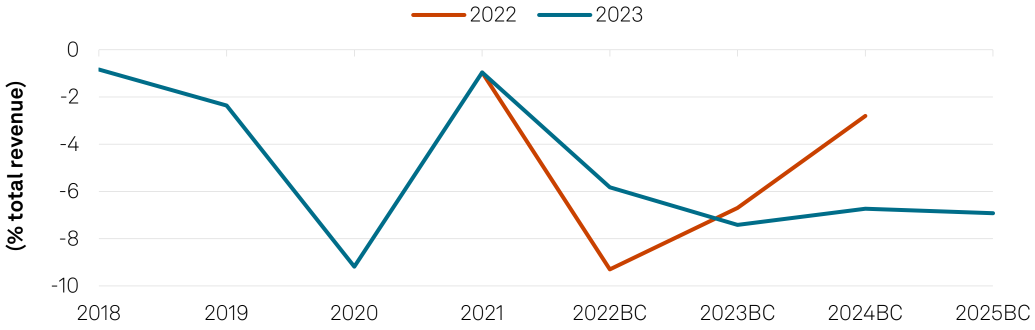
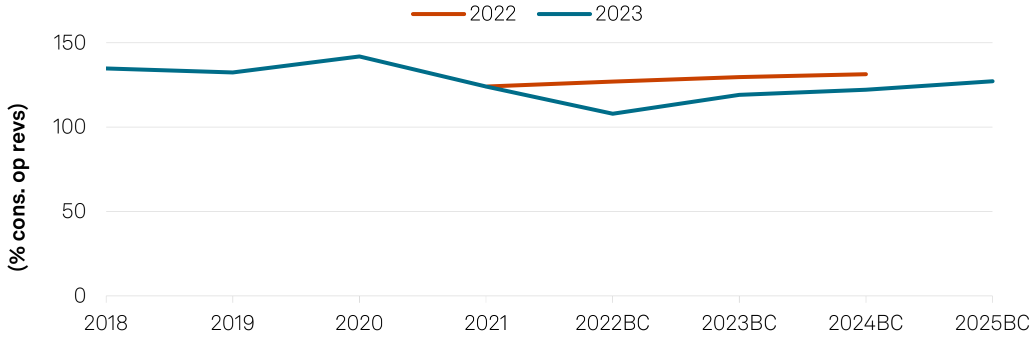
Nova Scotia

AA-/Stable/A-1+

Nova Scotia balance after capital accounts



Nova Scotia tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- Strong population growth supports economic activity, but also brings growing pains.
- Elevated projected capital spending will pressure after-capital results.
- We expect the province's debt burden to rise but remain one of the lowest among Canadian provinces.

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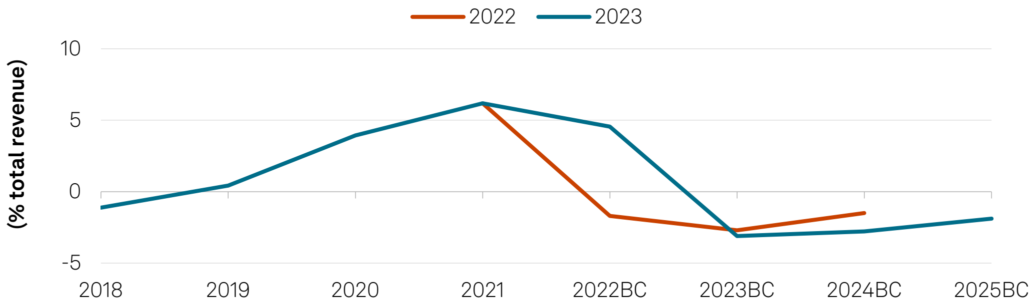
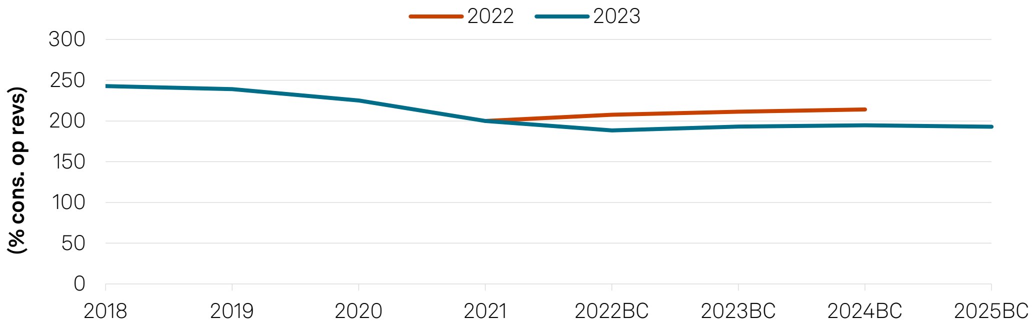
New Brunswick

A+/Positive/A-1+

New Brunswick balance after capital accounts



New Brunswick tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- Government's focus on fiscal restraint will keep operating balances healthy despite softening economic activity.
- Large projected capital spending could push after-capital balances into a modest deficit.
- New Brunswick’s liquidity position remains a key credit strength.

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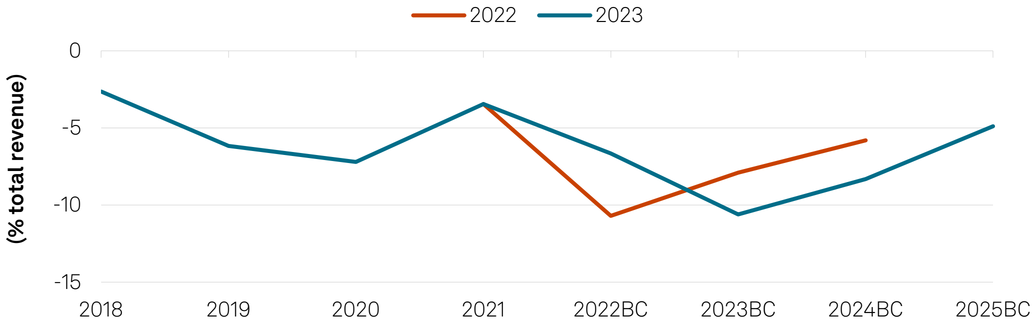
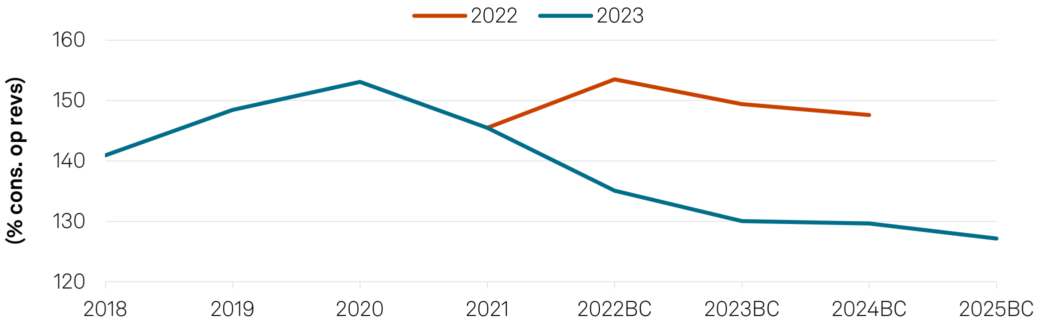
Prince Edward Island

A/Positive/A-1

Prince Edward Island balance after capital accounts



Prince Edward Island tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- Nation-leading population growth rate has fueled solid economic growth in the past several years.
- Consequently, we expect revenue growth in fiscal 2023 and 2024 will be robust, although performance has been offset by storm-related expenditures.
- Fiscal balance is achievable in the medium term despite recessionary risks and rising cost pressures.
- Infrastructure investments, in part to support the growing population, will increase nominal debt modestly although PEI's debt burden will remain among the lowest of Canadian provinces.

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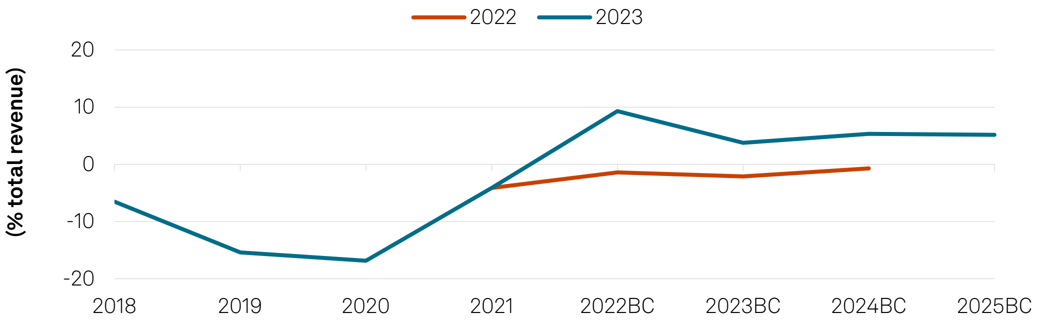
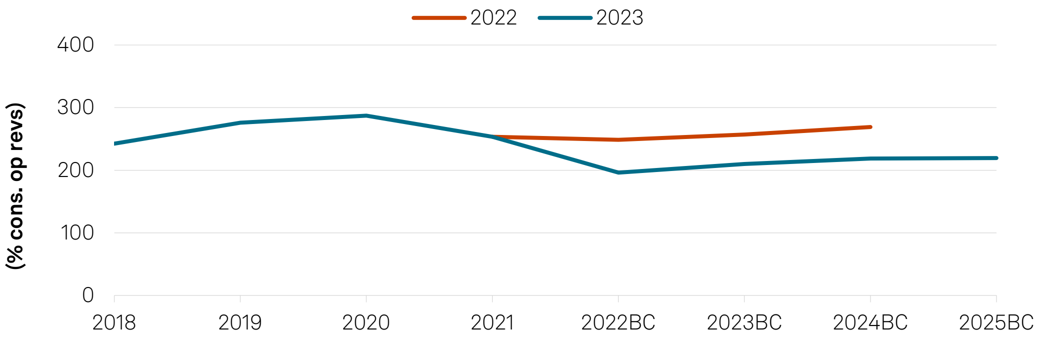
Newfoundland and Labrador

A/Stable/A-1

Newfoundland and Labrador balance after capital accounts



Newfoundland and Labrador tax-supported debt



Years correspond to budget years (fiscal year ending March 31 of following year).
BC--Base case. Source: S&P Global Ratings.

- Strong commodity prices will drive real GDP growth as private sector investment in the energy and mining sectors helps to mitigate near-term macroeconomic headwinds that are more pronounced than in other provinces.
- Stronger operating revenues will spur an accelerated improvement in the province’s budgetary performance as well as its debt burden, compared with the previous base case.
- Nevertheless, the province's fiscal results are significantly tied to the rise and fall of oil prices and its fiscal performance is very volatile compared with that of Canadian and global peers.

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