February 7, 2018 - (Vol. 2, No. 10)

Quick Hit — Ontario: Efficiency in motion

By all accounts, Tuesday was an exceptional day. Earlier equity carnage meant investor anxiety was through the roof, with volatility metrics all but off the charts. The closely watched VIX index had skyrocketed, reaching its highest point in at least a couple years. (A related tidbit: the XIV ETF, whose cash payment at scheduled maturity is based on the *inverse* performance of the S&P 500 VIX Short-Term Futures Index, saw its trading halted most of the morning and was down 93% as of the close.) Such was backdrop only 24 hours ago. But wild market gyrations didn't prevent Ontario from enjoying its own exceptional day, as the province tapped both the US dollar and domestic (C$) bond markets in good size, vaulting its fiscal year borrowing program miles beyond fully funded status. If your attention was fixed on the inter-day blips in the Dow Jones Industrial Average, here's what Ontario accomplished Tuesday:

- US$3 billion of a new 3-year benchmark SEC Registered Global (ONT 2.55% 02/12/2021). Having attracted excellent demand out of the gate (books approached US$4 billion from reports we heard), the deal was priced a snick tighter than IPT (albeit at somewhat attractive levels to the secondary USD Ontario curve). Ontario had last been in dollars back in September, and this represented the province's largest Global since May-2012. Based on the prevailing exchange rate, CAD-equivalent proceeds amounted to roughly C$3.75 billion. In terms of pricing, we pegged this deal some 7-8 bps "cheap" to Ontario's domestic curve (based on mid swaps). Technically, you could say that Ontario paid up a bit to access a very deep pool of liquidity south of the border. Importantly, however, the bond was not sufficiently "cheap" to entice investors to move out of short-dated C$ Ontario bonds into the new USD security.
- Just as this new 3-year USD bond was getting firmed up, Ontario popped a new 5-year benchmark bond into the domestic market (C$1.5 billion of the ONT 2.6% 09/08/2023). As with the dollar trade, this new domestic 5-year was on the larger side of the spectrum, having been launched in response to healthy expressions of interest. For reference, Ontario's previous domestic 5-year—ONT 1.35% 03/08/2022—was launched and re-opened (4 times) at C$1 billion a crack, resulting in a float of C$5 billion.

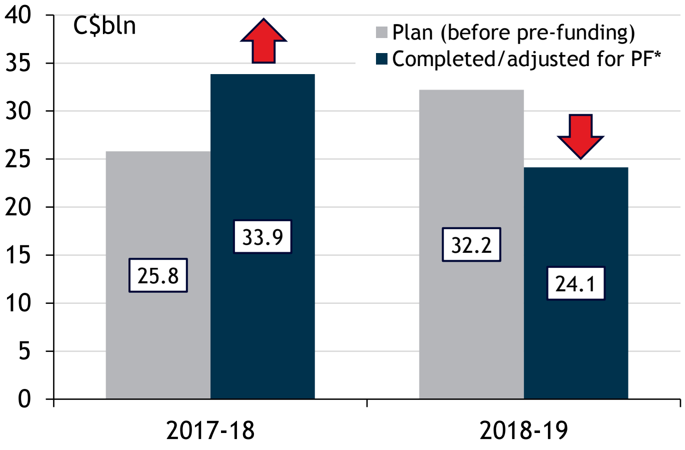
Together then, Ontario cleared some C$5.25 billion via two trades amidst a highly unstable global financial backdrop. If those proceeds sound outsized, they are, amounting to the largest single-day lift from Ontario since at least 2010 (perhaps ever). Consider this a vote of confidence by investors on either side of the border, notwithstanding some lingering risks (housing and NAFTA to name two). More to the point, Tuesday's one-two punch demonstrates just how efficient our large provincial issuers can be. For context, Ontario's *full-year* funding requirement for the 2017-18 fiscal year has been pegged at $25.8 billion. So the province just knocked off fully 20% of a full-year requirement in a single trading day. Here's another perspective: Ontario secured more funding on Tuesday than was raised during the entire month of January by all provinces together. Not too shabby.

And it's not like the province had been playing from its back foot. Ontario had already crossed the fully funded threshold well before Tuesday's exceptional issuance. Adding in the latest proceeds, Ontario now finds itself more than $8 billion pre-funded towards fiscal 2018-19… with more than a month and a half still to run on the outgoing fiscal year. It's not unreasonable to expect that Ontario could have at least $10 billion of the coming fiscal year's requirement already completed before April 1st rolls around. To us then, one the single biggest changes in the upcoming provincial budget will likely be a hefty downward adjustment in long-term funding requirements for 2018-19, relative to what had been previously telegraphed (Chart 1).

Ontario might not be able to do much about equity market anxiety, but its big-time pre-funding serves to dampen any supply anxiety attached to Canada's largest provincial borrower. [While our focus here was Ontario, we'd be remiss if we didn't mention that Québec is likewise way out in front of next fiscal year's bond program, having pre-funded roughly $6 billion and counting (Chart 2).]

Chart 1: Ontario gets jump start on 2018-19…

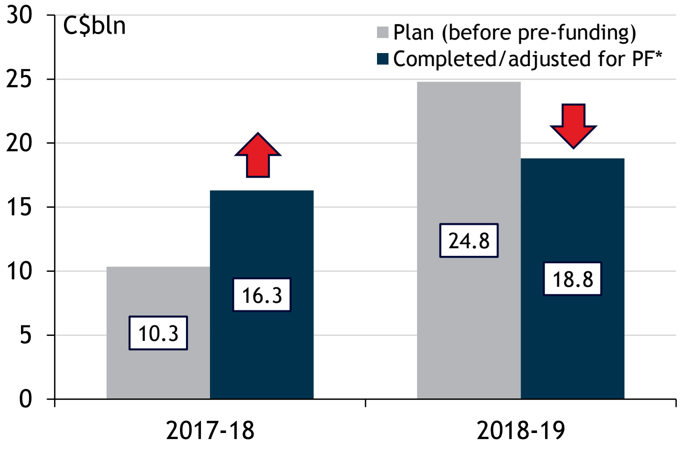
Ontario funding requirements: Official & adjusted for pre-funding



*Source: NBF, Ontario | * Official requirement less current pre-funding, subject to change/adjustment in upcoming provincial budget*

Chart 2: …and it's a similar story in Québec

Québec funding requirements: Official & adjusted for pre-funding



*Source: NBF, Québec | * Official requirement less current pre-funding, subject to change/adjustment in upcoming provincial budget*

Fixed Income Trading Desk Strategy

Public Sector Strategy
Warren Lovely
+1 416-869-8598 | Warren.Lovely@nbc.ca

Catherine Maltais
+1 514-879-8598 | Catherine.Maltais@nbc.ca

Taylor Schleich
+1 416-869-6480 | Taylor.Schleich@nbc.ca

Corporate Credit
Connor Sedgewick
+1 514-879-3182 | Connor.Sedgewick@nbc.ca

Pete Metzger
+1 416-869-8607 | Pete.Metzger@nbc.ca

Relative Value Models
Drew Lloyd
+44 (0)20-7488-9379 | Drew.Lloyd@nbc.ca

National Bank of Canada Financial Inc. (NBCFI), a broker-dealer registered with the U.S. Securities and Exchange Commission and a member of the Financial Industry Regulatory Authority (FINRA), and a member of the Securities Investor Protection Corporation (SIPC), is distributing this Report in the United States. NBCFI operates pursuant to a 15 a-6 Agreement with its Canadian affiliate, NBF Inc.

This Report has been prepared in whole or in part by personnel employed by non-US affiliates of NBCFI that are not registered as broker/dealers in the US. These non-US personnel are not registered as associated persons of NBCFI and are not licensed or qualified as research analysts with FINRA or any other US regulatory authority and, accordingly, may not be subject (among other things) to FINRA restrictions regarding communications by a research analyst with the subject company, public appearances by research analysts and trading securities held in a research analyst account.

The author(s) who prepared these Reports certify that this Report accurately reflects his or her personal opinions and views about the subject company or companies and its or their securities, and that no part of his/her compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed in this Report as to the securities or companies.

NBF compensates the authors of this Report from a variety of sources, and such compensation is funded by the business activities of NBF including, Institutional Equity and Fixed Income Sales and Trading, Retail Sales, the correspondent clearing business and Corporate and Investment Banking.

Because the views of its personnel may differ, members of the National Bank Financial Group may have or may in the future issue Reports that are inconsistent with this Report, or that reach conclusions different from those in this Report. To make further inquiry related to this Report, United States residents should contact their NBCFI registered representative.

This document is intended for institutional investors and is not subject to all of the independence and disclosure standards under FINRA rules applicable to debt research Reports prepared for retail investors. This Report may not be independent of the proprietary interests of NBF, NBCFI, or their affiliates. NBF, NBCFI, or their affiliates may trade the securities covered in this Report for their own account and on a discretionary basis on behalf of certain clients. Such trading interests may be contrary to the recommendation(s) offered in this Report.

HK Residents

With respect to the distribution of this email in Hong Kong by NBC Financial Markets Asia Limited ("NBCFMA") which is licensed by the Securities and Futures Commission ("SFC") to conduct Type 1 (dealing in securities) regulated activity, the contents of this email are solely for informational purposes. It has not been approved by, reviewed by, verified by or filed with any regulator in Hong Kong. Nothing herein is a recommendation, advice, offer or solicitation to buy or sell a product or service, nor an official confirmation of any transaction. None of the products issuers, NBCFMA or its affiliates or other persons or entities named herein are obliged to notify you of changes to any information and none of the foregoing assume any loss suffered by you in reliance of such information.

The content of this email may contain information about investment products which are not authorized by SFC for offering to the public in Hong Kong and such information will only be available to, those persons who are Professional Investors (as defined in the Securities and Futures Ordinance of Hong Kong ("SFO")). If you are in any doubt as to your status you should consult a financial adviser or contact us. This material is not meant to be marketing materials and is not intended for public distribution. Please note that neither this material nor the product referred to is authorized for sale by SFC. Please refer to product prospectus for full details.

There may be conflicts of interest relating to NBCFMA or its affiliates' businesses. These activities and interests include potential multiple advisory, transactional and financial and other interests in securities and instruments that may be purchased or sold by NBCFMA or its affiliates, or in other investment vehicles which are managed by NBCFMA or its affiliates that may purchase or sell such securities and instruments. No other entity within the National Bank of Canada group, including NBF, is licensed or registered with the SFC. Accordingly, such entities and their employees are not permitted and do not intend to: (i) carry on a business in any regulated activity in Hong Kong; (ii) hold themselves out as carrying on a business in any regulated activity in Hong Kong; or (iii) actively market their services to the Hong Kong public

Copyright