

Quebec confirms impressive fiscal momentum

By Warren Lovely

The Province of Quebec has done it again. Canada's second largest province (S&P: AA-, Moody's: Aa2, DBRS: AA (low), Fitch: AA-) has just released preliminary financial results for 2020-21. The results mark a significant improvement over what was telegraphed only a few weeks ago, the picture brightening even more materially relative to Quebec's March 2021 budget.

To be clear, Quebec still ran a deficit in 2020-21. There was a global pandemic after all, which radically affected revenue and spending patterns for all Canadian provinces (and virtually every government on the planet). Quebec now puts the 2020-21 deficit at C\$10 billion or 2.3% of provincial GDP. How does that stack up to prior guidance? It's better... in a big way.

Back on May 28th (as in less than four weeks ago), the 2020-21 deficit was pegged at C\$12 billion. This is a bit tongue in cheek, but a C\$2 billion improvement in roughly 4 weeks is akin to erasing one green banner (i.e., domestic benchmark bond deal) each week. Rewind the clock even further, to a March 25th budget, and you'll find the shortfall was estimated at C\$15 billion. In other words, the deficit has come down \$5 billion in the past three months. Nice.

To what does Quebec owe the fiscal improvement? For starters, economic activity held up better than expected. If you missed it, we explored Quebec's latest GDP release [here](#). How's this for a fun fact: Despite COVID-19, Quebec's own-source revenue actually grew last fiscal year (+0.6%). That's a pretty remarkable feat and speaks the underlying resilience of the domestic economy. Program spending, while up sharply vs. the pre-pandemic 2019-20 fiscal year, has nonetheless been marked down notably vs. prior guidance. We'd note that program spending adjustments may reflect capacity constraints (i.e., an inability to deploy funds as quickly as intended during the pandemic). Given the fiscal year is now over, residual contingencies/risk provisions can be released. That contributes C\$1.25 billion to the fiscal improvement relative to Budget 2021. Overall, this 'stronger revenue, lower program spending, lighter provisioning' narrative massively outstrips the extra ~C\$300 that flowed into the Generations Fund (which is earmarked for debt reduction).

So there you have it; Quebec ended 2020-21 with a deficit, yes, but there was one third less red ink than originally believed. All this implies a much healthier cash balance to start the 2021-22 fiscal year. Moreover, we see the stronger revenue base carrying over. Perhaps best of all, Quebec's nominal GDP is absolutely bounding higher in 2021. We last projected 11.9% nominal growth for 2021 vs. the 6% budget planning assumption. To us, this sets the stage for another, perhaps even bigger budget beat this fiscal year.

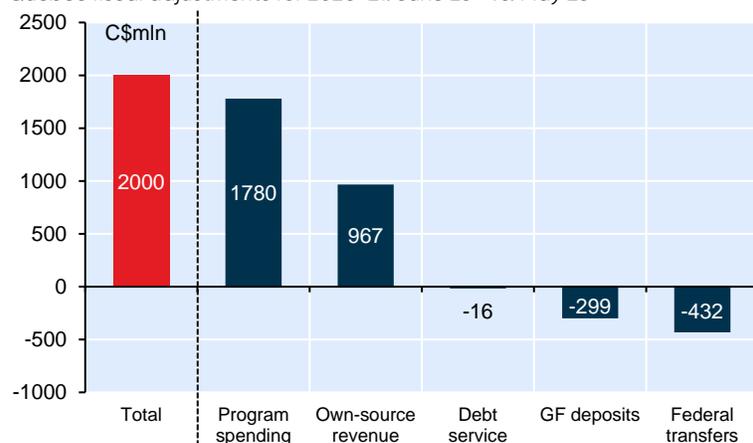
Again, these are unofficial fiscal results and won't be confirmed until the 2020-21 public accounts drop. But we've seen enough to know that Quebec's 2021-22 net financial requirement is likely to be materially lower than that telegraphed a few months back, all else equal. That creates scope for one serious reduction in official funding needs in future fiscal updates, meaning Quebec will likely get to fully funded status much quicker than expected. That in turn means greater flexibility to manage future bond issuance, simultaneously hinting at an ability to get a big chunk of pre-funding done way before the next fiscal year kicks off.

More fundamentally, an economic recovery is clearly translating into fiscal traction... not just in Quebec but across the country in our opinion. Sure, some of the improvement must be deemed cyclical, and in other parts of the country will owe a major assist to rising commodity prices. But after the events of the past year and a bit, this is a welcome fiscal improvement for Quebec specifically and Canada's provincial government sector more generally. It's a serious bit of fiscal momentum with real implications for provincial bond holders. So take notice.

Note: We released a detailed report on June 16th, entitled: "That's some serious couch money". That report outlined our detailed expectations for above-plan revenue in 2021-22 and beyond. We estimated C\$35 billion in 'found' money for Ottawa and the provinces this fiscal year, relative to what was planned for in 2021 budgets. This report can be accessed [here](#).

Chart 1: C\$2 billion better in less than a month...

Quebec fiscal adjustments for 2020-21: June 23rd vs. May 28th



Source: NBF, Quebec | Note: Positive values denote source of improvement

Chart 2: ... and a C\$5 billion improvement vs. Budget 2021

Quebec 2020-21 deficit 'waterfall': Path from Budget 2021 to latest estimate



Source: NBF, Quebec | Note: Blue bars denote change to deficit vs. Budget 2021

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