

Note to provincial bondholders: Search the merch

By Warren Lovely

Canada's latest monthly installment of merchandise trade dropped earlier today. Our colleague, Jocelyn Paquet, [provided insight](#) on the national details. Here we offer a complementary word on select provincial dimensions, keying on merchandise export trends. As is routinely the case, national figures mask major differences in regional performance. If anything, provincial performance gaps are getting bigger, not smaller, as price action and/or global supply chain kinks leave an indelible mark. Consider...

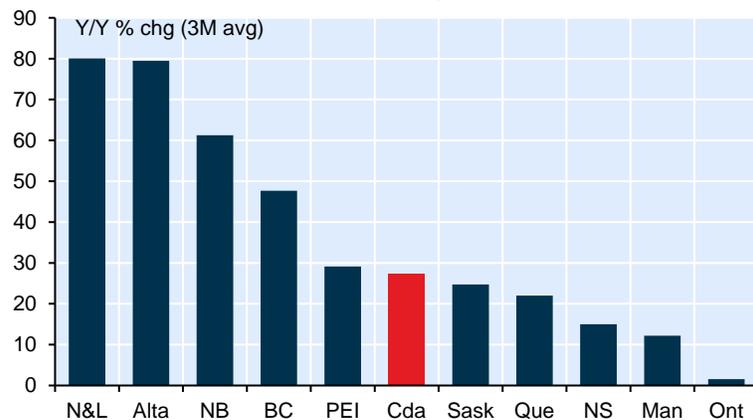
As of August, Canada's goods exports were up more than 25% year-on-year on a (three-month) smoothed basis. Domestic export growth was closer to +80% in Alberta and Newfoundland and Labrador (Chart 1), as the value of energy product shipments has absolutely exploded. Ontario sits at the other end of the spectrum, with goods exports up just 1.6% year-on-year. We're not hating on Ontario. Indeed, bondholders following our ongoing provincial fiscal/financial commentary will find a lot to like about Canada's largest province right now. Nonetheless, global chain issues are clearly weighing on the province's important auto sector, holding total provincial exports below pre-COVID levels. Looked at another way, if it weren't for autos, Ontario's merchandise exports would be up 12.5% year-on-year (Chart 2).

Meanwhile, Alberta's export surge, which is overwhelmingly but not entirely an energy story, has pushed the level of domestic exports some 25% above 2019 levels. This speaks to a monumental improvement in the terms of trade, which has likewise lit a fire under Alberta (and national) nominal GDP (see page 13 of [link](#)). Note that National Bank's detailed provincial economic forecast to be updated in the coming days.

Credit provincial bond investors for taking notice, as Alberta's basis to Ontario is hovering near the tightest levels since summer 2019 (Chart 3). Notwithstanding an outsized move in Alberta's basis of late (Chart 4), we're reluctant to call for a material near-term give back. Prospective primary market supply could conceivably limit further relative tightening, although Alberta (like some other provinces) appears relatively flush with cash at the moment. Moreover, with crude enjoying another leg higher of late, the value of Alberta energy exports, nominal GDP, oil royalties, overall government revenue and absolute/relative credit spreads should remain nicely supported here, which argues against selling the still-higher-yielding province short.

Chart 1: Provincial export growth highly uneven

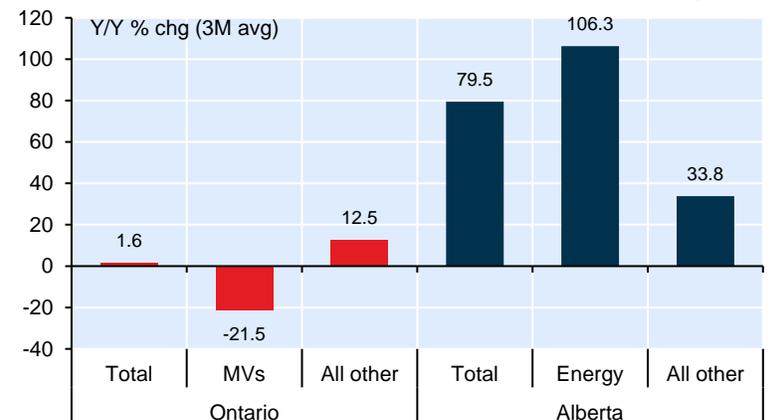
Growth in domestic exports by province (Aug-2021)



Source: NBF, StatCan | Note: Growth rates based on 3M average levels (Jun-Aug)

Chart 2: Ont/Alta & autos/energy divergence on full display

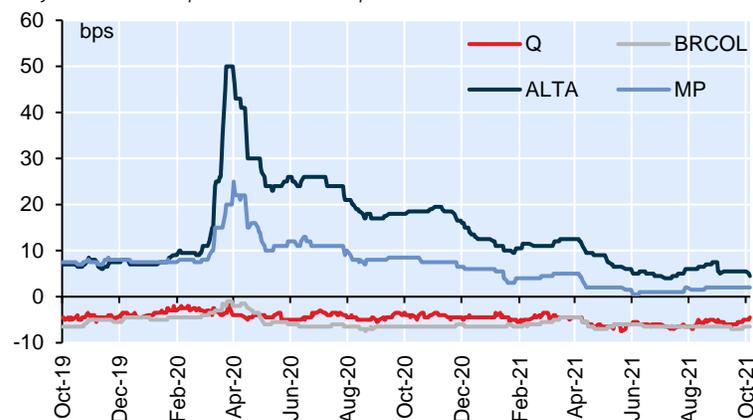
Growth in Ontario & Alberta domestic exports: Total & key sectors (Aug-2021)



Source: NBF, StatCan | Note: Growth rates based on 3M average levels (Jun-Aug)

Chart 3: Alberta credit spreads snug up nicely

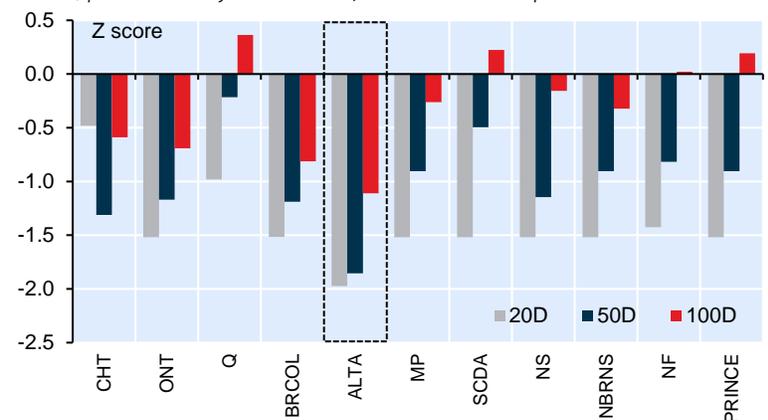
10-year indicative provincial credit spreads vs. Ontario



Source: NBF | Note: Based on daily constant maturity indications vs. Ontario

Chart 4: Alberta spreads at the limit?

Crown/provincial 10-year Z-scores, based on credit spreads vs. GoC curve



Source: NBF | Note: Based on daily constant maturity indications vs. GoC curve; Z scores represent # of SDs current spreads are relative to 20D, 50D & 100D averages



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