



Alberta's fiscal transformation does not go unnoticed

By Warren Lovely

Two months removed from Alberta's rather striking 2022 budget, this oil-intensive province was rewarded with a "Positive" outlook by Moody's. The brighter outlook is more than deserved in our opinion and reflects the monumental fiscal improvement that has been communicated over the past year or so (Chart 1). Budget 2022 places Alberta on track to balance the budget this fiscal year and that hardly looks like a stretch to us. As we've highlighted, Alberta and other resource-intensive provinces still look to have considerable revenue upside. In Alberta's case, there's perhaps scope for as much as \$10 billion in bonus revenue given where key commodity prices currently reside vs. planning assumptions.

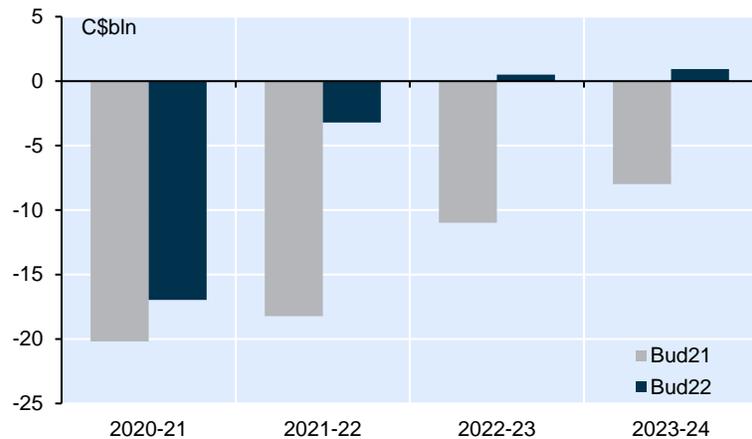
Now an outlook change is not to be confused with a full-blown rating upgrade. But given the scope for better-than-planned budget balances and even more forceful debt reduction, a Moody's upgrade is likely just a matter of time. It could perhaps follow the detailed fall/Q2 update? Forgive Alberta for savouring its recent good fortune, given that the province had earlier lost the equivalent of 12 rating notches across the four agencies that rate its debt since late 2015 (i.e., roughly three notches on average) (Chart 2).

One assumes the themes and rationale for rating uplift cited by Moody's have been picked up on at the other credit rating agencies too. So the Moody's boost is unlikely to be the only one. In terms of ratings location, S&P has been particularly harsh on Alberta, having cut a total of 5 notches since 2015 (i.e., AAA to A), leaving Alberta with a distinctly below-average rating at this particular agency (Chart 3).

As for market-related implications, we'd note that ratings (on their own) are a useful yet imperfect valuation tool. Their greatest utility is in valuing one province vs. another, with ratings currently explaining as much as two-thirds of domestic spread gaps. In Alberta's case, the basis spread to key provincial peers has been on an improving trajectory all year, a process that kicked into high gear in February as oil shot higher and the budget confirmed so much good news. Specifically, Alberta's 30-year basis to Ontario started 2022 at roughly +10 bps but today you'll find Alberta bonds trading at a slight premium (about 2 bps through). So investors don't necessarily require rating agencies to tell them what they already know, although formal confirmations of trading bias via rating/outlook changes doesn't hurt. Congrats Alberta!

Chart 1: Alberta's public finances monumentally better

Alberta budget balance outlook: Budget 2022 vs. Budget 2021



Source: NBF, Alberta

Chart 2: Bleeding over for Alberta credit rating

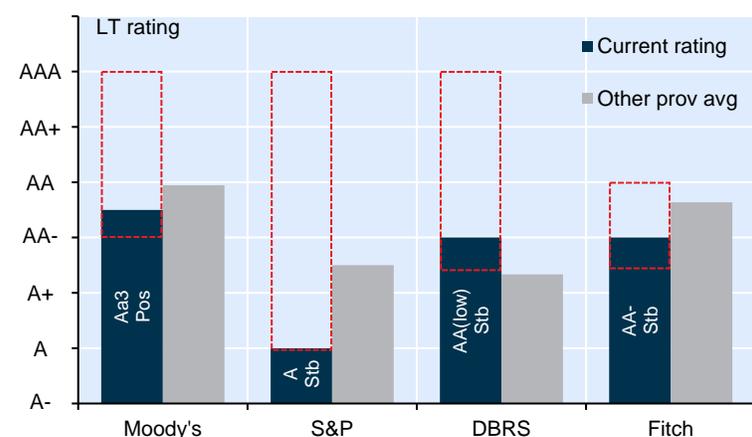
Alberta LT rating vs. Ontario & 10 province weighted avg over time



Source: NBF, Moody's, S&P, DBRS Morningstar | Note: Based on avg rating

Chart 3: Other +ve action(s) could come for Alberta

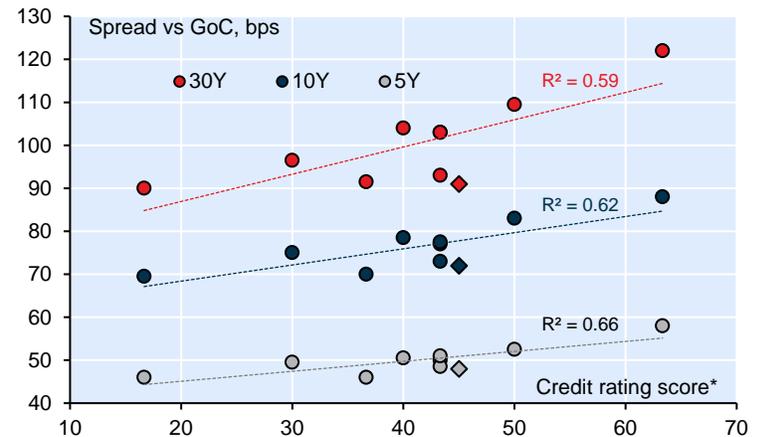
Alberta LT rating vs. historical rating range & simple avg of other provinces



Source: NBF, Moody's, S&P, DBRS Morningstar, Fitch | Note: Red box denotes Alberta's historical rating range at each agency; bars control for positive/negative outlooks

Chart 4: Ratings a useful although imperfect valuation tool

Relationship btw avg LT rating & provincial gov't domestic credit spreads



Source: NBF, Moody's, S&P, DBRS Morningstar | Note: Alberta denoted with diamond marker; credit rating score based on avg LT rating where AAA=10, AA+=20, AA=30, etc



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