

Quick Hit – Federal-provincial mid-year reporting wrap-up

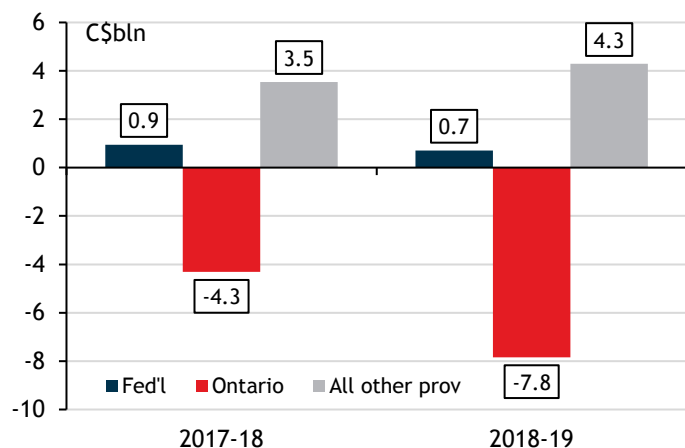
It may be the dying days of an entirely forgettable 2018, at least in terms of equity market and credit spread performance. But as late as Wednesday, we took receipt of the final mid-year updates for the 2018-19 fiscal year. For completeness then, we offer up this portrait of federal-provincial fiscal performance, keying on reported changes relative to the budgetary projections set down in the 2018 spring budget season. We'll keep our ramblings to a minimum and direct you to summary charts/tables.

In the overwhelming majority of cases, final adjustments to 2017-18 fiscal year results (via public accounts) *and* tweaks to the current, 2018-19 fiscal year figures (via in-year updates) have been positive. That sounds positive. Indeed, in the provincial government sector, the combined two-year budgetary position covering 2017-18 and 2018-19 has improved in nine of the ten provinces vs prior budget guidance. The notable exception has been Ontario, where a wholesale financial restatement followed June's general election (Charts 1-2)... a fiscal pivot/deterioration at a mature stage of an economic expansion that, not surprisingly, resulted in a recent credit rating downgrade for Canada's benchmark provincial credit by Moody's. Refer to our separate [short note](#) on that downgrade.

Four provinces are currently in surplus, but there's sufficient red ink in Ontario, Alberta and a few other corners (Chart 3) to produce an aggregate \$20.6 billion provincial deficit in 2018-19. [Note: there's a combined \$4 billion of prudence built into to current year forecasts, protection against a mounting list of financial market and real economy risks.] There's once more a larger combined deficit at the provincial level than there is federally, driving a larger wedge between federal-provincial debt burdens (Chart 4). That's the great fundamental force consistent with poorer average credit quality and wider average credit spreads in our provincial bond market. That's a tendency that needs to be reversed before growth sours materially and/or demographic pressures bite the provinces even harder. That road to fiscal recovery has to run through Ontario and Alberta, with 2019 looking like a pivotal year in both jurisdictions.

Chart 1: Fiscal revisionism a big story in Ontario

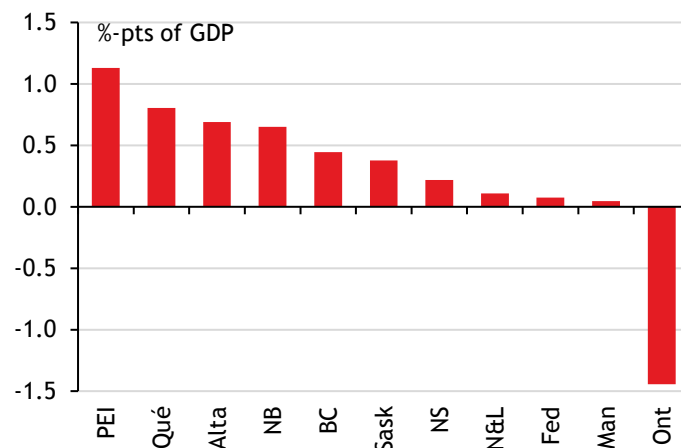
Change in budget balances: Actual/latest vs 2018 budget



Source: NBF, federal-provincial governments

Chart 2: Quantifying two-year fiscal adjustments

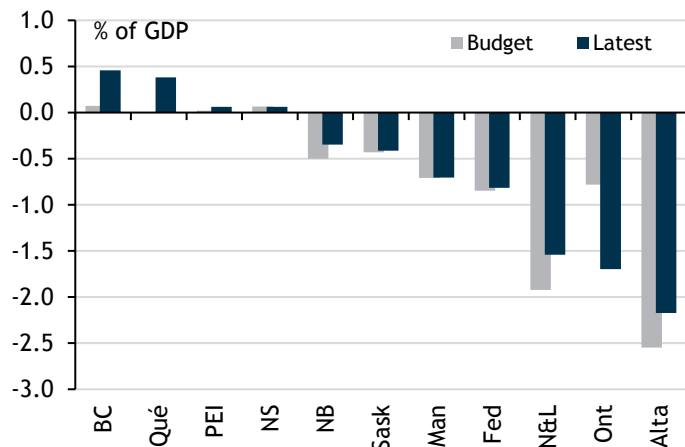
Cumulative chg in 2017-18 & 2018-19 budget balances vs 2018 budget



Source: NBF, federal-provincial governments

Chart 3: Budgetary snapshot... now vs budget

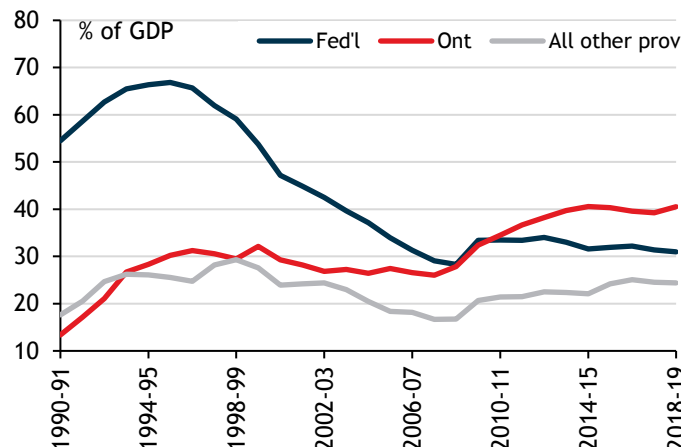
2018-19 budget balance as % of GDP: Latest vs 2018 budget



Source: NBF, federal-provincial governments

Chart 4: Evolution of net debt burdens

Federal-provincial net debt burdens over time



Source: NBF, federal-provincial governments

PLEASE SEE END OF DOCUMENT FOR IMPORTANT DISCLOSURES

Table: The finer details on budgetary adjustments
Federal-provincial budget balances: Actual/latest vs prior budget estimates/projections

Fiscal year >> Reference document >>		2017-18					2018-19				
		Bud 2017	Bud 2018	Latest	Chg17	Chg18	Bud 2017	Bud 2018	Latest	Chg17	Chg18
Budget balance (\$mln)											
Federal	GoC	-28,500	-19,900	-18,961	9,539	939	-27,400	-18,800	-18,100	9,300	700
Provincial total	Prov	-12,407	-9,537	-10,309	2,098	(772)	-11,187	-17,014	-20,569	(9,382)	(3,555)
– Excl. Ontario	ExOnt	-12,407	-10,179	-6,637	5,770	3,542	-11,187	-10,310	-6,025	5,162	4,285
– Most populous (Ont, Qué, BC)	Big-3	295	1,643	-749	(1,044)	(2,392)	244	-6,485	-11,544	(11,788)	(5,059)
– Oil-levered (Alta, N&L, Sask)	Oil-3	-11,807	-10,473	-9,237	2,570	1,236	-10,657	-9,850	-8,407	2,250	1,443
– Remaining provinces	Oth-4	-895	-707	-323	572	384	-774	-679	-618	156	61
Ontario	Ont	0	642	-3,672	(3,672)	(4,314)	0	-6,704	-14,544	(14,544)	(7,840)
Québec	Qué	0	850	2,622	2,622	1,772	0	0	1,650	1,650	1,650
– Underlying balance (excl GF)	QuéxGF	2,488	3,142	4,915	2,427	1,773	2,834	2,491	4,501	1,667	2,010
British Columbia	BC	295	151	301	6	150	244	219	1,350	1,106	1,131
Alberta	Alta	-10,344	-9,066	-8,023	2,321	1,043	-9,709	-8,802	-7,512	2,197	1,290
Manitoba	Man	-840	-726	-695	145	31	-698	-521	-518	180	3
Saskatchewan	Sask	-685	-595	-303	382	292	-304	-365	-348	(44)	17
Nova Scotia	NS	136	134	230	94	97	36	29	27	(8)	(2)
New Brunswick	NB	-192	-115	67	259	182	-117	-189	-131	(14)	57
Newfoundland & Labrador	N&L	-778	-812	-911	(133)	(99)	-644	-683	-547	97	136
Prince Edward Island	PEI	1	1	75	75	74	5	2	4	(1)	3
Contingencies / reserves (\$mln)											
Federal: adjustment for risk	GoC	3,000	0	0	(3,000)	0	3,000	3,000	3,000	0	0
Provincial total	Prov	2,750	750	0	(2,750)	(750)	2,185	3,585	4,282	2,097	697

Notes: Compiled by NBF, the above table compares official / government budget balance assumptions from 2017 & 2018 budgets with more recent estimates;

" Bud 2017 " refers to original budget balance projections from 2017 spring budgets; " Bud 2018 " refers to budget balance projections from 2018 budgets

Fixed Income Trading Desk Strategy

Public Sector Strategy

Warren Lovely

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

Catherine Maltais

+1 514-879-2270 | 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

Important Disclosures

General

This Report was prepared by National Bank Financial, Inc. (NBF), (a Canadian investment dealer, member of IIROC), an indirect wholly owned subsidiary of National Bank of Canada. National Bank of Canada is a public company listed on the Toronto Stock Exchange.

The particulars contained herein were obtained from sources which we believe to be reliable but are not guaranteed by us and may be incomplete and may be subject to change without notice. The information is current as of the date of this document. Neither the author nor NBF assumes any obligation to update the information or advise on further developments relating to the topics or securities discussed. The opinions expressed are based upon the author(s) analysis and interpretation of these particulars and are not to be construed as a solicitation or offer to buy or sell the securities mentioned herein, and nothing in this Report constitutes a representation that any investment strategy or recommendation contained herein is suitable or appropriate to a recipient's individual circumstances. In all cases, investors should conduct their own investigation and analysis of such information before taking or omitting to take any action in relation to securities or markets that are analyzed in this Report. The Report alone is not intended to form the basis for an investment decision, or to replace any due diligence or analytical work required by you in making an investment decision.

Any opinions expressed herein reflect a trading perspective. NBF, or its affiliates may publish fundamental research on the subject issuer(s), which may reflect a different opinion. This Report is not produced by the NBF Research Department and has not been reviewed by the NBF Research Department.

This Report is for distribution only under such circumstances as may be permitted by applicable law. This Report is not directed at you if NBF or any affiliate distributing this Report is prohibited or restricted by any legislation or regulation in any jurisdiction from making it available to you. You should satisfy yourself before reading it that NBF is permitted to provide this Report to you under relevant legislation and regulations.

National Bank of Canada Financial Markets is a trade name used by National Bank Financial and National Bank of Canada Financial Inc.

National Bank Financial Inc. or an affiliate thereof, owns or controls an equity interest in TMX Group Limited ("TMX Group") and has a nominee director serving on the TMX Group's board of directors. As such, each such investment dealer may be considered to have an economic interest in the listing of securities on any exchange owned or operated by TMX Group, including the Toronto Stock Exchange, the TSX Venture Exchange and the Alpha Exchange. No person or company is required to obtain products or services from TMX Group or its affiliates as a condition of any such dealer supplying or continuing to supply a product or service.

Canadian Residents

NBF or its affiliates may engage in any trading strategies described herein for their own account or on a discretionary basis on behalf of certain clients and as market conditions change, may amend or change investment strategy including full and complete divestment. The trading interests of NBF and its affiliates may also be contrary to any opinions expressed in this Report.

NBF or its affiliates often act as financial advisor, agent or underwriter for certain issuers mentioned herein and may receive remuneration for its services. As well NBF and its affiliates and/or their officers, directors, representatives, associates, may have a position in the securities mentioned herein and may make purchases and/or sales of these securities from time to time in the open market or otherwise. NBF and its affiliates may make a market in securities mentioned in this Report. This Report may not be independent of the proprietary interests of NBF and its affiliates.

This Report is not considered a research product under Canadian law and regulation, and consequently is not governed by Canadian rules applicable to the publication and distribution of research Reports, including relevant restrictions or disclosures required to be included in research Reports.

UK Residents

This Report is a marketing document. This Report has not been prepared in accordance with EU legal requirements designed to promote the independence of investment research and it is not subject to any prohibition on dealing ahead of the dissemination of investment research. In respect of the distribution of this Report to UK residents, NBF has approved the contents (including, where necessary, for the purposes of Section 21(1) of the Financial Services and Markets Act 2000). This Report is for information purposes only and does not constitute a personal recommendation, or investment, legal or tax advice. NBF and/or its parent and/or any companies within or affiliates of the National Bank of Canada group and/or any of their directors, officers and employees may have or may have had interests or long or short positions in, and may at any time make purchases and/or sales as principal or agent, or may act or may have acted as market maker in the relevant investments or related investments discussed in this Report, or may act or have acted as investment and/or commercial banker with respect hereto. The value of investments, and the income derived from them, can go down as well as up and you may not get back the amount invested. Past performance is not a guide to future performance. If an investment is denominated in a foreign currency, rates of exchange may have an adverse effect on the value of the investment. Investments which are illiquid may be difficult to sell or realise; it may also be difficult to obtain reliable information about their value or the extent of the risks to which they are exposed. Certain transactions, including those involving futures, swaps, and other derivatives, give rise to substantial risk and are not suitable for all investors. The investments contained in this Report are not available to retail customers and this Report is not for distribution to retail clients (within the meaning of the rules of the Financial Conduct Authority). Persons who are retail clients should not act or rely upon the information in this Report. This Report does not constitute or form part of any offer for sale or subscription of or solicitation of any offer to buy or subscribe for the securities described herein nor shall it or any part of it form the basis of or be relied on in connection with any contract or commitment whatsoever.

This information is only for distribution to Eligible Counterparties and Professional Clients in the United Kingdom within the meaning of the rules of the Financial Conduct Authority. NBF is authorised and regulated by the Financial Conduct Authority and has its registered office at 71 Fenchurch Street, London, EC3M 4HD.

NBF is not authorised by the Prudential Regulation Authority and the Financial Conduct Authority to accept deposits in the United Kingdom.

U.S. Residents

With respect to the distribution of this report in the United States of America, National Bank of Canada Financial Inc. ("NBCFI") which is regulated by the Financial Industry Regulatory Authority (FINRA) and a member of the Securities Investor Protection Corporation (SIPC), an affiliate of NBF, accepts responsibility for its contents, subject to any terms set out above. To make further inquiry related to this report, or to effect any transaction, United States residents should contact their NBCFI registered representative.

This report is not a research report and is intended for Major U.S. Institutional Investors only. This report is not subject to U.S. independence and disclosure standards applicable to research reports.

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) and Type 3 (leveraged foreign exchange trading) regulated activities, 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 National Bank of Canada and National Bank Financial Inc, 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

This Report may not be reproduced in whole or in part, or further distributed or published or referred to in any manner whatsoever, nor may the information, opinions or conclusions contained in it be referred to without in each case the prior express written consent of NBF.