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Ontario: Longer lasting deficit to safeguard economy

By Warren Lovely, Taylor Schleich, Daren King and Ethan Currie

Highlights

With economic uncertainty continuing to weigh on the economy, Budget 2026 sees the provincial government renew its pledge to protect Ontario. In this ambitious fiscal plan, the province seeks to defend workers and businesses from ongoing economic uncertainty, while strengthening global competitiveness through corporate tax relief, infrastructure investment, affordability measures, and expanded public service. Paramount to this plan is the establishment of the Protect Ontario Account Investment Fund (POAIF), which will deploy up to $4 billion in public seed capital, aiming to attract private investment into strategic sectors and bolster long-term economic prospects. Looking back, the 2025-26 deficit ($12.3 billion or 1.0% of GDP) was smaller than outlined in Budget 2025 and the Fall Economic Statement. However, the deficit will grow marginally in 2026-27 as the province now plans for a $13.8 billion (1.1% of GDP) shortfall—the largest since 2020-21. In these highly uncertain times, Ontario's alternative fiscal scenarios are particularly informative. These imply the 2026-27 deficit could conceivably land between $11.2 billion and $16.6 billion, depending on the evolution of the Canada-U.S. trade relationship. While protecting Ontario will be costly in the coming fiscal year, the province has outlined a plan to quickly tackle the deficit over the following two years. However, this return to balance has been delayed by a year compared to earlier guidance. Ontario now expects to run a $6.1 billion (0.5% of GDP) shortfall in 2027-28 before registering a modest $0.6 billion surplus in 2028-29. While this budgetary path requires restrained spending (~1% growth per year), considerable prudence is built into the fiscal plan between sub-consensus GDP growth assumptions, $6 billion in reserves (across the plan horizon) and a $3 billion contingency fund. Ontario's net debt is estimated to have reached $459 billion in the outgoing fiscal year, as the net-debt-to-GDP ratio was revised down to 36.8% due to stronger nominal GDP. Roughly $70 billion in additional net debt in the next three years will push this ratio to a projected peak of 38.5% in 2027-28 before it begins to decline, remaining below the 40% threshold in the base case. Debt-to-revenue is expected to stay above its 200% guideline through the fiscal framework, though accounting changes and medium-term consolidation should help to restore compliance here by the early 2030s. Meantime, debt servicing remains manageable in our view, even with projected rises in borrowing costs. The province issued a near-record $58.6 billion in term debt in 2025-26, taking advantage of strong demand (domestically, and overseas). Strategic prefunding was well absorbed and aided in the launch of the POAIF. Looking ahead, borrowing is set to decelerate to $47.2 billion in 2026-27 and step down further to an average of ~$43 billion in the following two fiscal years. Issuance will be increasingly diversified into international currencies, with a remaining focus on developing a deep / liquid CAD benchmark program and a sustained presence in green bond supply.

- **Economic outlook** —2025 posed significant challenges to Ontario's economy. First, trade uncertainty and sector-specific tariffs, particularly in the automotive sector, weighed heavily on the province's growth. Furthermore, changes in immigration policy led to a significant slowdown in population growth, which had a particularly significant impact on Ontario given its high proportion of non-permanent residents. Consequently, Ontario's GDP grew by only 1.2% in 2025, which was slower than the 1.6% growth in 2024 and the 1.7% recorded at the national level. However, this growth rate is higher than the 0.8% projected in last year's budget and the fall economic update, as the impact of US tariffs was less significant than initially feared. Regarding nominal GDP, which has a greater impact on public finances, growth of 4.2% is estimated for 2025. This is higher than the 3.1% and 3.2% initially projected in the previous budget and fall update, but slightly lower than the 4.3% observed nationally. In terms of population growth, Ontario experienced one of the most significant slowdowns among Canadian provinces, dropping from 3.3% in 2024 to 0.7% in 2025. Furthermore, the most recent data from early 2026 indicates that the population declined by 0.7% compared to January 1st, 2025 — an unprecedented situation. Consequently, non-permanent residents as a share of the population fell from a peak of 9.1% in Q3:2024 to 7.4% in Q4:2025. Employment growth also slowed significantly, dropping from 1.7% in 2024 to 1.0% in 2025. As a result, Ontario has seen the sharpest deterioration in its unemployment rate of all the provinces, rising from 7.0% in 2024 to 7.7% in 2025, and is now the province with the highest jobless rate west of Atlantic Canada. 2025 was also marked by a widespread slump in Ontario's real estate market. Indeed, transactions in the resale housing market fell by 5.6% from 2024 to 2025, while housing starts dropped from 71,800 to 65,400 units—the largest decline in both absolute and relative terms among all Canadian provinces.

  Looking ahead, the budget is based on weaker economic growth in 2026, with real GDP rising by just 1.0%, as demographic headwinds and trade uncertainty continue to weigh on growth. This forecast is just below the 1.1% average forecast by private-sector economists, but above our own forecast of 0.6%. The economy is expected to regain momentum in subsequent years, with real GDP growth projected at 1.7% in 2027, 1.9% in 2028 and 2.0% in 2029 (all figures are one tenth of a percentage point below the average forecast by private-sector economists). As for nominal GDP, the growth rate is also expected to be lower in 2026, coming in at 3.2%, notably due to a lower deflator. However, surprises regarding inflation could cause this figure to increase (for example, if the conflict in the Middle East continues for an extended period). Nominal GDP is then expected to grow faster in subsequent years: 3.9% in 2027, 3.7% in 2028 and 3.9% in 2029. Regarding the labour market, job creation in 2026 is expected to be half that of the previous year at 0.5%, before rising to 0.7% in 2027, 0.8% in 2028, and 1.1% in 2029. Nevertheless, this would result in a decline in the unemployment rate, given that employment growth would outpace population growth. Indeed, the unemployment rate is expected to fall from 7.7% in 2025 to 7.4% in 2026 and then to 6.9% and 6.4% in 2027 and 2028, respectively. The budget does not include any forecasts in regard to population growth, but our own projections suggest a decline of 0.8% in 2026, followed by modest increases of 0.2% in 2027 and 0.6% in 2028. As for the housing market, the budget projects a 9.1% rebound in resale transactions in 2026, which we consider an optimistic assumption given the weak momentum observed year-to-date. Meantime, the pace of housing starts is expected to remain extremely low in 2026 at just 64,800 units, a level relatively unchanged from 2025. Construction is then expected to accelerate to 70,300 units in 2027 and 76,800 units in 2028.

- **New initiatives** — Budget 2026 is building on initiatives introduced last year when economic uncertainty surged. In fact, the title of the 2026 budget—A Plan to Protect Ontario—is unchanged from last year, as the province seeks to "build the most competitive, resilient, and self-reliant economy in the G7". It's not a short-winded plan, as program expenses total $687.3 billion over the next three fiscal years. Efforts are once again concentrated on: (1) protecting workers and businesses and (2) bolstering global economic competitiveness. Across these broader themes, Budget 2026's new measures are laid out as a five-pronged approach, which aims to (1.a) protect workers and businesses from tariffs and economic uncertainty, (2.a) invest in infrastructure via "the most ambitious provincial capital plan in Canadian history", (2.b) expand and improve key services, (2.c) improve affordability, and (2.d) ensure the safety of Ontario's borders and communities. Punchline—Ontario plans to play defence and offence. See below for more details on specific measures.
  - *Protecting Workers and Businesses*: Ontario is delivering on its Tax Action Plan to bolster global economic competitiveness and lower costs through several avenues. Combined tax relief of almost $2.2 billion is slated through the removal of the HST for all eligible buyers of new homes valued at up to $1.5 million (a maximum rebate of $130K) in a federal-provincial cost sharing mechanism. The Budget also plans to cut the small business corporate income tax (CIT) rate from 3.2 percent to 2.2 percent effective July 1st, 2026. This would provide over 375,000 provincial small businesses with an additional $1.1 billion in CIT relief over the next three years. A fresh $107 million is allocated to renew support for the Critical Technologies Initiatives program. Funding here will help to accelerate the development, commercialization, and adoption of key technologies in key sectors. The establishment of the Protect Ontario Account Investment Fund (POAIF) will also aim to bolster investment in these economic and sectoral priorities, such as advanced manufacturing, automotive, life sciences, military, critical minerals, and artificial intelligence. We discuss the Fund in more detail below. The province also intends to lower the cost of capital investments by allowing businesses to accelerate the tax deductions for the cost of depreciable assets, in alignment with policies announced at the federal level.
  - *Protecting Ontario*: The "most ambitious provincial capital plan in Canadian history" outlines more than $210 billion in planned investment over the next decade, including $37 billion in the upcoming fiscal year. This sum includes monies allocated to building highways, hospitals, transit, and other essential community infrastructure to support the Ontarian workforce and broader economy for future generations. The province will provide an additional $300 million over the next six years through the Community Sport and Recreation Infrastructure Fund, while also working with the federal government to enhance the process of funding directed to eligible municipalities, reducing development charges while simultaneously making housing more affordable, and construction timelier. Ontario also intends to bring forward legislation that would see it head the governance of Toronto's Billy Bishop Airport, with the goal to support its future growth and expansion in an economically beneficial manner. In continued effort to connect every Ontarian to a primary care provider, the province is expanding its four-year investment in the Primary Care Action Plan to $3.4 billion from 2025 to 2029. Healthcare-related expenditures are set to expand at an average annual rate of over 4% throughout the Budget's horizon. That's higher than aggregate spending growth, as health care remains a focus in Ontario and across Canada (as seen from other provincial budgets through similarly focused investment in the field). More specifically, approximately $64 billion is earmarked for health infrastructure over the next decade (of which ~$50 billion is capital grants). This funding will support over 50 hospital projects and deliver approximately 3,000 new hospital beds to enhance system efficiency and capacity. Nearly $140 million is allocated in additional funding to support quality long-term care. On the education front, Ontario will invest roughly $30 billion across the ten-year capital plan to support the (re)development and modernization of school, learning spaces, and childcare projects. Nearly $70 million per school year will be invested to create the Classroom Supplies Fund for elementary school teachers, ensuring the reduction of out-of-pocket expenses for necessary education supplies/equipment. A new long-term investment model will bring an additional $6.4 billion to support access to the postsecondary education sector, raising annual operating funding to $7 billion (a 30% increase and the highest level on record). In other efforts to keep costs down, the province will extend the Ontario One Fare Program for another two years, saving daily transit users in the GTHA up to $1,600 per year. The Budget also proposes new consumer protection measures that will make it illegal for tickets to live entertainment events (sports, concerts) to be resold for more than their original cost. In the document's final section, the province outlines its plans to protect borders and communities by investing $32.5 million in the upcoming fiscal year as part of Operation Deterrence 2.0 to address border-related enforcement gaps. Ontario will also expand the capacity of the adult correctional system, invest more than $41 million in School Resource Officer programs over the next three years, and provide an additional ~$8 million to support police / bail services in 2026-27.
  - *Additional Details on the Protect Ontario Account Investment Fund (POAIF)*: Here's where the province is playing offence. The establishment of the POAIF will seed up to $4 billion to attract domestic investment from, and in partnership with the private sector. This contribution will fulfill the province's $5 billion commitment as it pertains to the Protect Ontario Account introduced in last year's budget. Through partnership with a private investment manager (the general partner is yet to be disclosed), this fund will identify and execute on a pipeline of investment opportunities that align with the province's economic and strategic priorities. Acting as a limited partner in this economic relationship, Ontario will seek to promote and maintain strong public governance of the fund, ensuring that its activities are beneficial to both the province and that it acts as a profitable/attractive venture to other partners. By leveraging private sector expertise and capital, Ontario will seek to advance on the development of key sectors in an accelerated fashion otherwise unattainable with provincial funding alone. Public seed capital will thus act as a 'carrot' in this context, drawing in capital from key institutional investors to deliver "a clear benefit to Ontario taxpayers", avoiding potential alternatives whereby domestic players may be forced into Canadian-based investment.
- **Latest estimate of the 2025-26 budget balance** — In Budget 2025, the province forecasted a $14.6 billion deficit for 2025-26, and by the time the Fall Economic Statement was released, the expected shortfall moderated to $13.5 billion. This was little changed in the Q3 report but since then, the bottom line has improved further. Ontario now expects to run a $12.3 billion deficit (1.0% of GDP) for 2025-26 with the final budget balance to be confirmed via public accounts data later this year. The budgetary beat relative to the FES is mostly a function of the province releasing $1.5 billion of the $2.0 billion reserve set aside for the year. Revenues did come in stronger by $3.5 billion (+1.6%) but that was offset by $3.8 billion in additional spending (+1.6%). Within spending, the health sector accounts for the bulk of the in-year pressures.

- **Upcoming fiscal year outlook (2026-27)** — 2025-26's shortfall may have come in better than earlier guidance, but the 2026-27 fiscal outlook has deteriorated. Ontario is now guiding towards a $13.8 billion deficit (1.1% of GDP) in the fiscal year starting next week. That's slightly larger than the $12.3 billion shortfall for the outgoing fiscal year but is up more materially compared to a Budget 2025 estimate of $7.8 billion and an FES projection of $7.7 billion. In 2026-27, revenue is expected to increase by 2.3%, which is only a hair below the pace of spending growth (2.4%). That means the reserve is the main driver of the year-over-year deficit increase. Here, Ontario has set aside $1.5 billion in 2026-27 for budgetary flexibility which is down from the $2.0 billion reserve contained in last year's budget.
- **Medium-term outlook (2027-28 and 2028-29)** — Ontario continues to telegraph a path to balance over its three-year fiscal plan, but this has been delayed by a year relative to Budget 2025 and the Fall Economic Statement. Rather than achieving balance in 2027-28, the province now expects to run a $6.1 billion deficit (0.5% of GDP). That's seen giving way to a modest surplus of $0.6 billion (0.0% of GDP) in 2028-29. In both years, there's substantial prudence in the form of a $2.0 billion reserve in 2027-28 and a $2.5 billion reserve in 2028-29. The return to balance is function of strong revenue growth (+4.7% per year) outpacing a restrained pace of spending (+1.4% per year). Program spending will be even more tightly contained, rising just 0.9% per year over this horizon. With the return to balance delayed by a year, it means that more red ink will accumulate than previously envisioned. From 2025-26 to 2027-28 (the "overlapping" years of the Budget 2025 and Budget 2026), the cumulative deficit has risen from $22 billion to $32 billion. However, if you include last fiscal year (2024-25), slippage in the cumulative deficit is more modest (moving from $28 billion to $33 billion).
- **Alternative fiscal scenarios** — Thanks to a disrupted Canada-U.S. trade relationship and now, a war in the Middle East, economic uncertainty remains elevated. Credit to Ontario for once again detailing faster and slower growth scenarios and the resulting impact on key fiscal metrics. In the faster growth scenario, most tariffs and countermeasures imposed by the U.S. and Canada are removed in the near term and economic growth is stronger in 2026 and 2027. Ontario estimates this scenario would result in an $11.2 billion deficit in 2026-27, a tiny $0.7 billion deficit in 2027-28 and an $8.5 billion surplus in 2028-29. The slower growth scenario assumes the U.S. withdraws from CUSMA and imposes tariffs of 12% on Canada (with some natural resource exports exempted). Under these circumstances, Ontario would not return to balance by 2028-29. Instead, the province projects deficits of $16.6 billion, $12.7 billion and $8.3 billion over the next three fiscal years (through 2028-29). Note that the budget's economic assumptions were locked in as of January, so there are no scenarios relating to a prolonged conflict in Iran with sharply higher oil prices.
- **Contingencies, prudence & official sensitivities** — Consistent with past practice, the budget incorporates meaningful prudence across a few dimensions. This includes baseline budgetary assumptions on the back of conservative GDP growth forecasts (set 0.1%-pt below the consensus in all cases). Reserves accounting is also notable—the $6 billion cumulatively set aside over the duration of the fiscal plan ($1.5 billion in 206-27, $2 billion in 2027-28, and $2.5 billion in 2028-29) is in line with what was included in the previous year's budget, and comfortably above what the province has opted for in the past. There's another important buffer in the form of a standard contingency fund, amounting to $1.5 billion for 2026-27 and increasing further throughout the medium-term outlook. All told, we consider this meaningful prudence—outright and by relative provincial standards. Official fiscal sensitivity analysis suggests a 1%-pt 'surprise' on nominal GDP growth is worth ~$1.25 billion in total taxation revenue per year. On the expense side, it's believed that a 1%-pt upward parallel shift in Ontario borrowing rates would add approximately $870 million to the interest bill in year one.
- **Debt outlook & interest bite** — Ontario's net debt is projected to have ended 2025-26 at $459 billion. While that was little changed compared to the level flagged in November's FES, an upgraded take on nominal GDP means the closely watched net debt-to-GDP ratio is marked down to 36.8% (vs. 37.7% in FES). With the serious actions to protect the economy leading to larger and longer-lasting deficits, alongside the ongoing push to deliver strategic capital investments, roughly $70 billion of net debt will be added in the coming three fiscal years. That will keep the debt burden rising in the near-term. The net debt-to-GDP ratio is projected at 37.7% for 2026-27, with a peak level of 38.5% forecast one year later (2027-28), before turning lower in the final year of the plan (2028-29). This fresh planning projection respects the pledge/aim to keep net debt-to-GDP below 40%. Note: Under a 'slower growth scenario', net debt-to-GDP would reach the 40% threshold by 2027-28, but in the same vein a faster growth scenario could essentially keep this ratio moving sideways in the coming two years. While Ontario's planning projection for the net debt-to-revenue ratio follows a broadly similar pattern to net debt-to-GDP, this particular leverage metric is currently above the 200% target and expected to remain so throughout the fiscal framework. Debt-to-revenue is projected to rise to 211% in 2026-27, peaking at 213% in 2027-28. Despite the notional breach of the intended threshold, "the government remains committed to and has proven it has the capability to reattain this target". It's believed that the 200% debt-to-revenue target could be achieved by 2032-33 (one year later than the timeline estimated in Budget 2025). Note that new accounting rules for net debt, coming into effect for 2026-27, will provide a degree of relief relative to the outgoing methodology. The province estimates that the accounting change permanently lowers the net debt-to-GDP ratio by 0.8%-pts and the net debt-to-revenue ratio by ~4%-pts, all else equal. Sensibly, Ontario also targets the 'interest bite' or the share of revenue consumed by interest on debt (IOD). The baseline outlook (or planning projection) sees the interest bite rising from 6.3% in 2025-26 to 7.1% by 2028-29—consistently below the 7.5% limit. The IOD profile factors in an expectation of higher borrowing costs, as the average borrowing rate is projected to rise from 3.85% in 2025-26 to 4.3% for each of 2027-28 and 2028-29. IOD is Ontario's fourth largest expense item, and without trivializing the ~7% compound average annual growth in interest/debt servicing charges over the three-year forecast horizon, we continue to view Ontario's debt load as relatively affordable. The current level is not far off the lowest levels seen since the 1980s. As a reminder, Ontario's interest bite averaged 8-9% in the decade leading up to the COVID pandemic (to say nothing of the 14-15% levels routinely registered during the 1990s). Like net debt-to-GDP, it would likely take a slower growth scenario to eventually push the province above its self-imposed target for the IOD-to-revenue ratio.
- **Borrowing requirement** — Taking full advantage of robust investor demand, at home and increasingly abroad, Ontario issued $58.6 billion of long-term debt in 2025-26. That was more than $15 billion higher than originally projected in Budget 2025, driven by what we view as a prudent decision to prefund a strategic initiative and a portion of the coming fiscal year's underlying requirement. Specifically, the extra 2025-26 issuance covers the marginal financing needed to establish the innovative Protect Ontario Account Investment Fund (discussed earlier). The outgoing year's bond crop was second only to the $59.8 billion that was raised during the peak of the pandemic in 2020-21. Of the total amount raised, the equivalent of $23.9 billion or just over 40% was sourced from international markets (USD, EUR, CHF). That was a larger foreign currency share

than the 20-35% originally projected and was the highest since in/around the GFC. As noted, Ontario's prefunding efforts leave marginal cash to be drawn upon from here. Moreover, evident demand for Ontario's money-market paper should allow for a $6 billion increase in short-term outstandings in each of the coming two fiscal years. That would leave $47.2 billion in long-term issuance planned for 2026-27 and ~$43 billion (on average) in the following two fiscal years. All else equal, the borrowing plan would imply a deceleration from the relatively rapid long-term borrowing pace set in 2025-26. With foreign investor demand for Ontario bonds expected to persist, the province aims to source 20-40% from international markets. The province points out that international funding has been relatively cost-effective vs. domestic markets, highlighting the net savings achieved on a 30-year EUR bond offering vs. the prevailing domestic cost of funds (on a hedged basis). Despite the marginal tilt towards international markets, preserving/maintaining deep, liquid domestic benchmarks remains a demonstrated priority—and something of a hallmark for this frequent issuer. Ontario is an unquestioned leader in the Green Bond space and once again commits to bringing multiple Green Bonds each fiscal year.

- **Current long-term credit ratings** — S&P: AA-, Stable | Moody's: Aa3, Stable | DBRS: AA, Stable | Fitch: AA-, Stable

  *[Refer to our **Provincial Ratings Snapshot** for additional colour on specific credit rating drivers/considerations]*

Details of Ontario's Fiscal Plan

($ Billions)

	Actual	Interim	Medium-Term Outlook		
	2024–25	**2025–26**	**2026–27**	**2027–28**	**2028–29**
Revenue					
Personal Income Tax	55.7	61.9	65.1	69.5	74.1
Sales Tax	39.4	39.2	39.9	43.2	45.1
Corporations Tax	27.8	27.6	28.6	30.6	32.5
Ontario Health Premium	5.2	5.2	5.5	5.7	5.9
Education Property Tax	5.9	5.9	6.0	6.0	6.1
All Other Taxes	17.6	18.0	18.5	19.1	20.1
Total Taxation Revenue	**151.5**	**158.0**	**163.6**	**174.1**	**183.8**
Government of Canada Transfers	36.6	39.1	39.8	40.1	40.4
Income from Government Business Enterprises	7.5	7.3	6.5	6.8	7.3
Other Non-Tax Revenue	30.5	22.2	21.9	22.4	22.6
Total Revenue	**226.2**	**226.6**	**231.9**	**243.4**	**254.1**
Programs					
Health Sector	91.3	97.8	101.2	103.5	106.7
Education Sector[1]	38.3	40.5	40.8	41.2	41.5
Postsecondary Education Sector	14.2	14.0	14.0	12.8	12.7
Children, Community and Social Services Sector	20.5	21.5	21.4	21.6	21.7
Justice Sector	7.2	7.3	7.3	7.3	7.4
Other Programs	40.6	41.2	42.4	42.5	41.3
Total Programs	**212.1**	**222.4**	**227.0**	**229.0**	**231.3**
Interest and Other Debt Servicing Charges	15.1	16.0	17.2	18.6	19.7
Total Expense	**227.3**	**238.4**	**244.2**	**247.5**	**251.1**
Surplus/(Deficit) Before Reserve	**(1.1)**	**(11.8)**	**(12.3)**	**(4.1)**	**3.1**
Reserve	–	0.5	1.5	2.0	2.5
Surplus/(Deficit)	**(1.1)**	**(12.3)**	**(13.8)**	**(6.1)**	**0.6**
Net Debt as a Per Cent of GDP[2]	35.7%	36.8%	37.7%	38.5%	38.2%
Net Debt as a Per Cent of Revenue[2]	191.2%	204.4%	210.9%	212.9%	209.8%
Interest as a Per Cent of Revenue	5.5%	6.3%	6.7%	6.9%	7.1%

[1] Excludes Teachers' Pension Plan. Teachers' Pension Plan expense is included in Other Programs.
[2] For 2026–27 and future years, Net Debt reflects financial assets less financial liabilities and is aligned with Net Financial Liabilities, as will be reported in the *Public Accounts of Ontario 2026–2027*. See the Debt Burden Reduction Strategy in Chapter 4: *Borrowing and Debt Management* for additional details on the calculations supporting the ratios.
Note: Numbers may not add due to rounding.
Sources: Ontario Treasury Board Secretariat and Ontario Ministry of Finance.

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Subscribe to our publications:
NBC.EconomicsStrategy@nbc.ca

To contact us:
514-879-2529

Stéfane Marion
Chief Economist and Strategist
stefane.marion@nbc.ca

Matthieu Arseneau
Deputy Chief Economist
matthieu.arseneau@nbc.ca

Jocelyn Paquet
Senior Economist
jocelyn.paquet@nbc.ca

Kyle Dahms
Senior Economist
kyle.dahms@nbc.ca

Alexandra Ducharme
Senior Economist
alexandra.ducharme@nbc.ca

Daren King, CFA
Senior Economist
daren.king@nbc.ca

Warren Lovely
Chief Rates and Public Sector Strategist
warren.lovely@nbc.ca

Taylor Schleich
Rates Strategist
taylor.Schleich@nbc.ca

Ethan Currie
Strategist
ethan.currie@nbc.ca

Angelo Katsoras
Geopolitical Analyst
angelo.katsoras@nbc.ca

Nathalie Girard
Senior Coordinator
n.girard@nbc.ca

Giuseppe Saltarelli
Desktop Publisher
giuseppe.saltarelli@nbc.ca

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