

January 27, 2026 – (Vol. X, No. 12)

Provincial credit quality on the defensive?

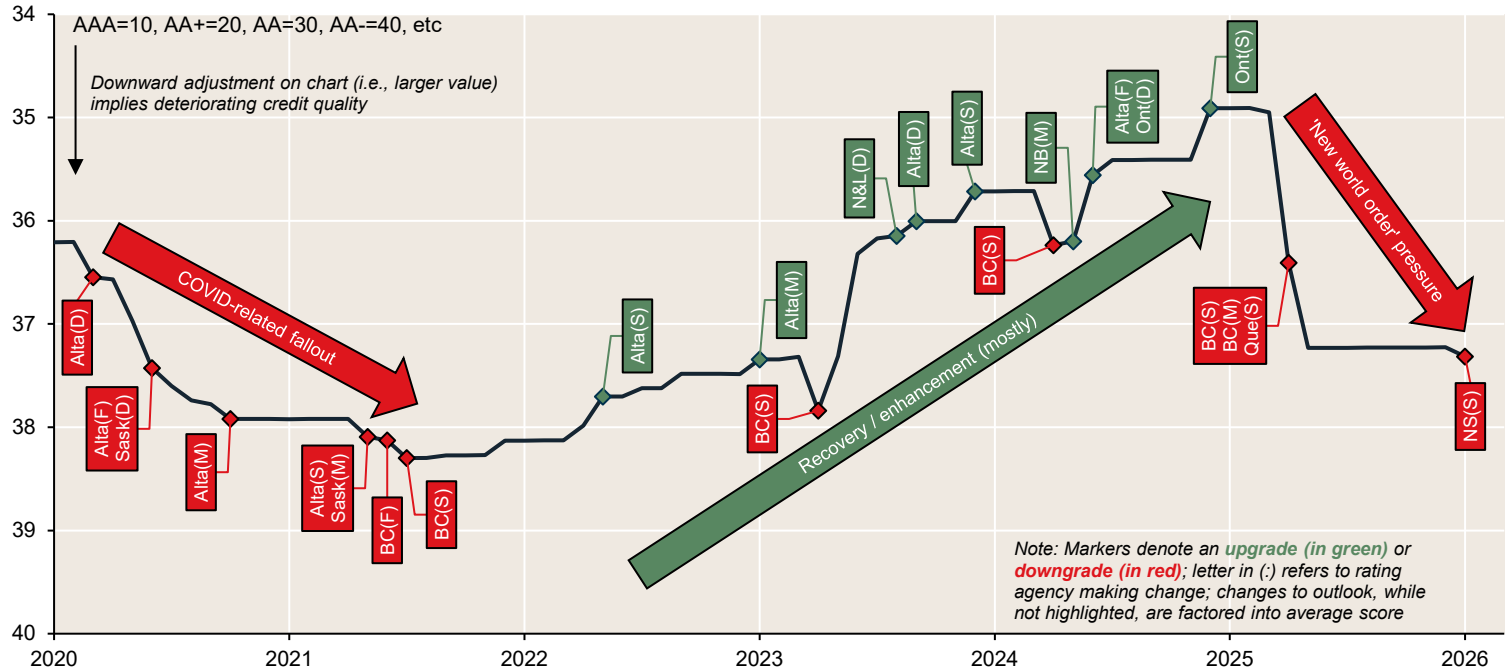
By Warren Lovely

The 2026 provincial budget season hasn't even started, yet the first rating downgrade has landed. Specifically, S&P downgraded Nova Scotia a single notch from 'AA-' to 'A+', maintaining a 'negative' outlook. Rather than unpacking this specific downgrade, we put provincial rating trends in

perspective. As to whether credit ratings even matter to investors, statistical analysis answers in the affirmative... at least when it comes to where provinces trade one vs. the other. Granted, relative liquidity counts for much, while political risk is a growing consideration for some.

Chart 1: Evolution of average provincial credit quality... from COVID pandemic through recovery to a 'new world order'

Weighted average provincial long-term credit rating score (CRS)

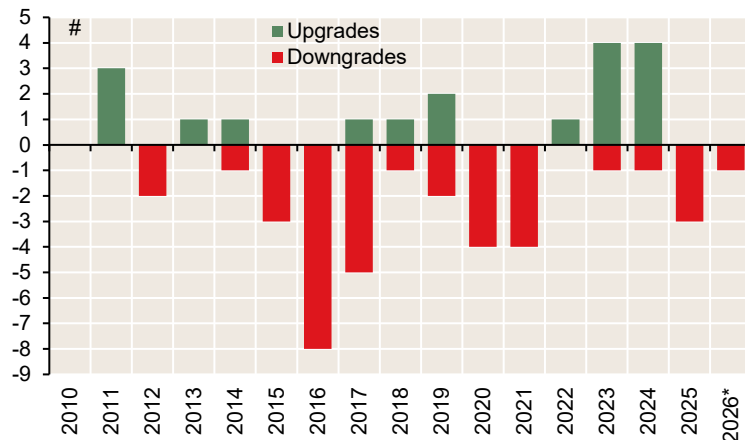


Source: NBC, S&P, Moody's, DBRS, Fitch, StatCan | Note: CRS is linear transformation of rating, controlling for outlook; re-weighted monthly using working age population; up to 27-Jan-26

On January 26th, S&P downgraded the Province of Nova Scotia a single notch from 'AA-' to 'A+', maintaining a 'negative' outlook. As per S&P, the downgrade reflected a "weaker budgetary position". Mind you, fiscal pressure is hardly unique to Nova Scotia, helping to explain why the weighted average provincial credit score has mostly given up the ground won during a post-COVID recovery. There will be much to digest in the upcoming budget season, but we expect provincial finances to remain under some strain. So this may not be the only negative rating adjustment delivered in 2026.

Chart 2: Counting upgrades & (more recently) downgrades

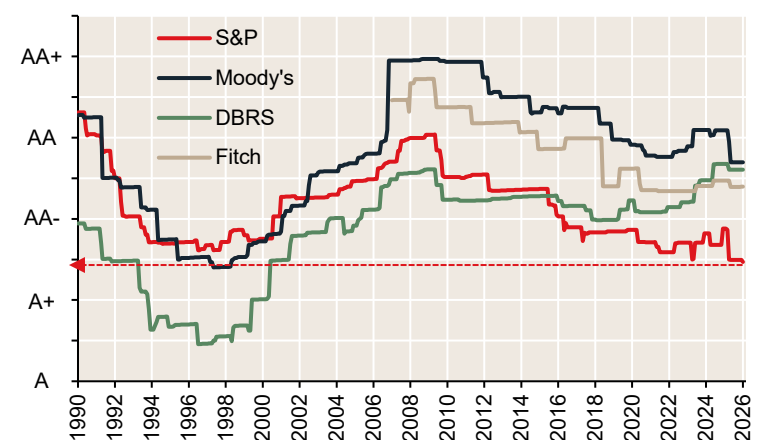
Count of provincial long-term credit rating upgrades & downgrades



Source: NBC, S&P, Moody's, DBRS, Fitch | Note: 2026 is up to 27-Jan; simple count of number of rating notch upgrades and downgrades each calendar year

Chart 3: S&P relatively more bearish (and/or proactive)

Weighted average provincial long-term credit rating by agency

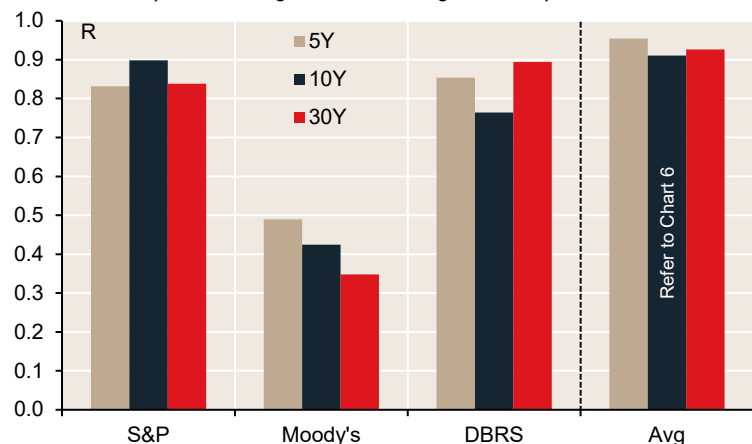


Source: NBC, S&P, Moody's, DBRS, Fitch, StatCan | Note: 2026 is up to 27-Jan; re-weighted monthly based on working age population; Fitch avg starts 2007 & currently covers 5 provs

Building on three 2025 downgrades, the N.S. move highlights a deteriorating balance of provincial rating adjustments. At present, five of 35 provincial ratings are on 'negative' outlook, implying some risk of further ratings pressure after 2026 budgets are presented. Stay tuned. Of the major rating agencies, S&P has been more decisive (some might say proactive or bearish) when it comes to the provinces. Indeed, the weighted average rating S&P assigns to the provincial sector is now lower than at any time since 1990. At Moody's, by contrast, ratings pressure has much more contained.

**Chart 4: Which set of ratings fits best with provi spreads?**

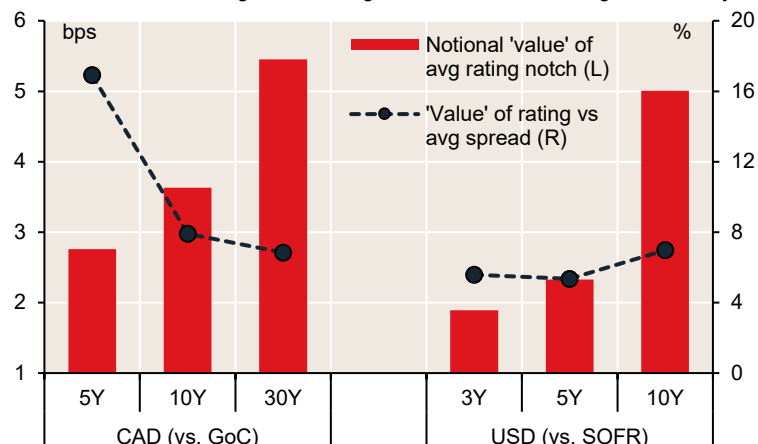
Correlation btw provincial long-term credit ratings & CAD spreads vs. GoC



Source: NBC, S&P, Moody's, DBRS | Note: Correlation between current ratings (controlling for non-stable outlooks) & CAD spread indications by tenor; as of 27-Jan-26

Chart 5: How much is a rating 'worth'? [Interpret with caution]

Estimated value of average credit rating notch, based on OLS regression analysis



Source: NBC, S&P, Moody's, DBRS, BBG | Note: OLS regression of current spread indications on average credit rating score, relative liquidity & political risk dummy; as of 27-Jan-26

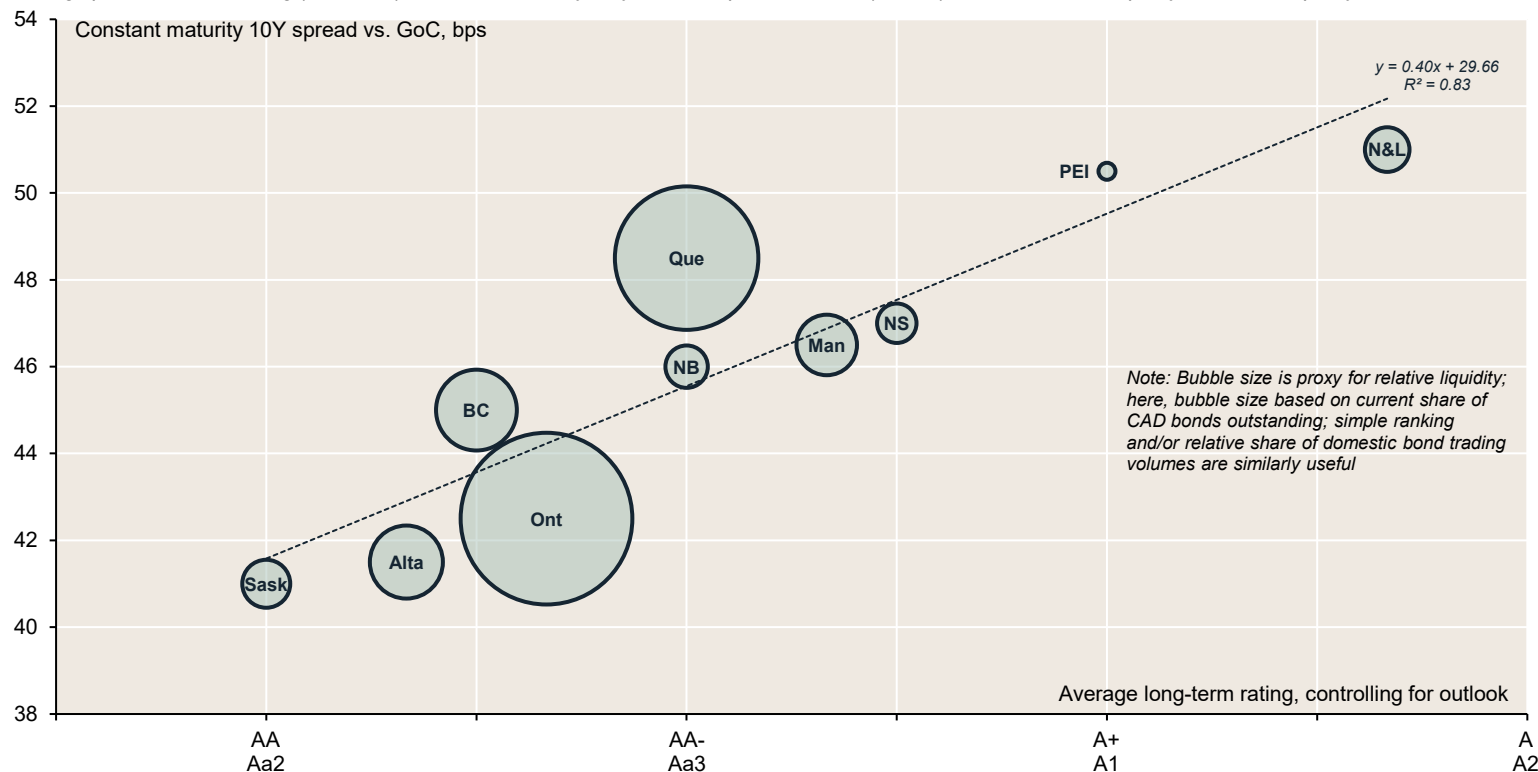
Time to ask the question: Do credit ratings even matter to provincial spreads? Not surprisingly, the answer is nuanced. Notwithstanding weaker budgetary performance and accumulating debt at the provincial level, Canada's federal government is leveraging up at an even faster rate. From a fundamental and technical perspective then, relative budget balances, debt trajectories and net bond supply dynamics support today's tight provincial spreads vs. the GoC curve. (To say nothing of the apparent wall of cash actively seeking marginal yield/carry across credit markets globally.)

Where ratings are arguably most useful is when valuing one province vs. another. It's still the case that ratings alone explain much of the dispersion in provincial spreads. Granted, some sets of ratings appear more useful than others. For example, provincial spreads are currently far more correlated with S&P rating scores than with the equivalent set of ratings assigned by Moody's.

As for how much a single rating notch might be 'worth', OLS regressions incorporating (among other things) ratings, liquidity and (if so inclined) political risk provide a rough guide. In the domestic bond market, each notch on an average rating might be worth ~5 basis points in the 30Y sector. Note that the ratings coefficient can be expected to expand/compress with the overall level of spreads. Given this, an average rating notch may be worth 7-8% of the underlying spread in CAD 10s or 30s (a higher ratio in 5s given tight underlying spreads). That is NOT to say a given rating change elicits that magnitude of re-pricing. Alas, markets are efficient and investor attitudes adjust more swiftly than credit ratings. But do credit ratings matter? Statistically speaking, they absolutely do.

Chart 6: Snapshot of provincial credit spreads suggests ratings matter (a lot)... as does liquidity and political risk too!

Average provincial credit rating (horizontal) & constant maturity 10-year CAD spread vs. GoC (vertical), with bubble size a proxy for relative liquidity: 27-Jan-26



Source: NBC, S&P, Moody's, DBRS | Note: Snapshot based on current spreads & ratings/outlooks; for each province, three ratings are averaged (with outlooks controlled for)

The above chart focuses on 10-year provincial spreads in the domestic (CAD) market. Vertically, we plot constant maturity indications vs. the GoC curve as of January 27th. A given province's average credit rating is expressed horizontally. Here, we use the simple average of the three ratings assigned by each of S&P, Moody's and DBRS, controlling for non-stable outlooks. (We exclude Fitch since they rate only half the provinces.) At present, average credit rating scores explain 83% of the differentiation in 10Y G-spreads. You can improve fit by controlling for relative liquidity (using simple rankings, outstanding bond stocks or secondary trading volumes). While not always relevant, political risk is an increasing consideration for some and may help explain current Quebec bond valuations. Putting it all together, average rating scores *plus* relative liquidity *plus* a political risk dummy can yield a R-squared as high as 97%. Relatively simple, yet arguably quite effective.

**Excerpt: NBC's Provincial Ratings Snapshot as of 27-Jan-26 | Refer to our comprehensive Government Fact Sheet set for detailed notes**

			Ontario	Quebec	British Columbia	Alberta	Manitoba	Saskatchewan	Nova Scotia	New Brunswick	Newfoundland & Labrador	Prince Edward Island
Ticker	Bloomberg bond ticker	Govt	ONT	Q	BRCOL	ALTA	MP	SCDA	NS	NBRNS	NF	PRNCE
	Bloomberg T-bill ticker	Gteed	OHYD	QHELFINQUE		ALBCAP			NSMFC	NBMFC	NFLABINFMF	
		Govt	ONTB	QTB		ALTATB	MPTB		NVSCFB	NWBRTB	NFTB	
S&P	Long-term rating		AA-	A+	A+	AA-	A+	AA	A+	A+	A	A
	Outlook		Stable	Stable	Negative	Stable	Stable	Stable	Negative	Stable	Stable	Stable
	Short-term rating		A-1+	A-1	A-1	A-1+	A-1	A-1+	A-1	A-1+	A-1	A-1
	Stand-alone credit profile (SACP)		aa-	a+	a+	aa-	a+	aa	a+	a+	a	a
	Institutional framework		Very predictable & well-balanced — Applies to all provinces equally									
	Economy	20%	V Strong	V Strong	V Strong	Strong	V Strong	V Strong	Average	Average	Average	Strong
	Financial management	20%	Strong	Strong	Strong	Strong	Strong	Strong	Strong	Strong	Strong	Strong
	Budgetary performance	20%	Weak	V Weak	V Weak	Average	Average	Weak	V Weak	Average	Average	V Weak
	Liquidity	20%	Exceptional	Exceptional	Adequate	Exceptional	Strong	Exceptional	Adequate	Exceptional	< Adequate	Adequate
Moody's	Debt burden	20%	High	V High	High	High	High	Moderate	High	High	V High	High
	Date of rating report		19-Jun-25	16-Apr-25	2-Apr-25	8-May-25	26-May-25	5-Jun-25	26-Jan-26	8-Apr-25	21-Jul-25	1-May-25
	Long-term rating		Aa3	Aa2	Aa1	Aa2	Aa2	Aa1	Aa2	Aa1	A1	Aa2
	Outlook		Stable	Stable	Negative	Stable	Stable	Stable	Stable	Stable	Stable	Stable
	Short-term rating		P-1	P-1	P-1	P-1	P-1	-	-	-	-	-
	Systemic risk assessment		Aaa — Applies to all provinces equally, based on Government of Canada rating									
	Baseline Credit Assessment: Indicated assign		a1 a1	a1 aa3	aa3 aa2	aa3 aa3	a2 aa3	aa2 aa2	aa3 aa3	aa2 aa2	a2 a3	a1 a1
	F1: Economy	25%	3.64	4.22	3.56	3.31	4.10	2.96	5.23	5.87	3.86	4.89
	Regional income	15%	2.06	3.04	1.94	0.51	3.83	0.93	4.71	4.78	1.43	4.15
Morningstar DBRS	Economic growth	5%	9.00	9.00	9.00	6.00	6.00	6.00	9.00	9.00	6.00	6.00
	Economic diversification	5%	3.00	3.00	3.00	9.00	3.00	6.00	3.00	6.00	9.00	6.00
	F2: Inst'l framework/governance	30%	2.00	1.00	2.00	3.50	3.50	2.00	1.00	1.00	2.00	2.00
	Institutional framework	15%	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
	Governance	15%	3.00	1.00	3.00	6.00	6.00	3.00	1.00	1.00	3.00	3.00
	F3: Financial performance	20%	5.00	7.66	9.29	6.03	7.94	6.87	8.10	4.93	7.00	7.42
	Operating margin	10%	7.28	9.66	12.20	5.50	12.03	9.91	8.62	6.53	7.02	8.20
	Liquidity ratio	5%	4.42	10.33	11.75	12.11	4.69	6.67	12.14	3.65	10.97	10.27
	Ease of access to funding	5%	1.00	1.00	1.00	1.00	3.00	1.00	3.00	3.00	3.00	3.00
Fitch	F4: Leverage	25%	12.75	11.39	8.14	8.85	13.58	9.26	8.05	9.10	14.70	9.10
	Debt burden	15%	12.91	10.65	8.49	8.53	14.97	9.74	7.26	9.03	13.53	7.83
	Interest burden	10%	12.52	12.51	7.62	9.32	11.50	8.54	9.23	9.20	16.45	11.00
	Preliminary BCA scorecard-indicated outcome		5.70 (a2)	5.74 (a2)	5.38 (a1)	5.29 (a1)	7.06 (a3)	5.03 (a1)	5.24 (a1)	5.03 (a1)	6.64 (a3)	5.58 (a2)
	Idiosyncratic notching		-	-	-	-	-	+1	-	+1	-	-
	Operating environment notching		+1	+1	+1	+1	+1	+1	+1	+1	+1	+1
	BCA scorecard-indicated outcome		4.70 (a1)	4.74 (a1)	4.38 (aa3)	4.29 (aa3)	6.06 (a2)	3.03 (aa2)	4.24 (aa3)	3.03 (aa2)	5.64 (a2)	4.58 (a1)
	ESG Credit Impact Score (CIS)	1-5 (Pos-Neg)	CIS-2	CIS-2	CIS-2	CIS-2	CIS-2	CIS-2	CIS-2	CIS-2	CIS-3	CIS-2
	Environmental score (E)	1-5	E-3	E-2	E-3	E-4	E-3	E-3	E-3	E-3	E-4	E-3
Fitch	Social score (S)	1-5	S-2	S-3	S-2	S-2	S-2	S-2	S-3	S-2	S-3	S-2
	Governance score (G)	1-5	G-2	G-1	G-2	G-2	G-2	G-1	G-1	G-1	G-2	G-2
	Date of rating report		28-May-25	18-Jun-25	10-Apr-25	16-May-25	21-Aug-25	31-Jul-25	14-May-25	5-May-25	26-Aug-25	3-Sep-25
	Long-term rating		AA	AA(Low)	AA(High)	AA	A(High)	AA(Low)	A(High)	A(High)	A	A
	Outlook		Stable	Stable	Negative	Stable	Stable	Stable	Stable	Stable	Stable	Stable
	Short-term rating		R-1(High)	R-1(Mid)	R-1(High)	R-1(High)	R-1(Mid)	R-1(Mid)	R-1(Mid)	R-1(Mid)	R-1(Low)	R-1(Low)
	Strengths		Large, diversified economy	Large, diversified economy	Diversified economy	Competitive tax regime	Diversified & resilient economy	Responsible fiscal policy commitment	Economic stability	Political commitment to fiscal discipline	Significant energy resources	Relatively stable economy
	Challenges		Capacity to raise revenue	Low-cost hydro power generation	Fiscal capacity	Strong demographics	Demographics	Young & growing population	Prudent debt mgmt & structure	Significant liquidity via sinking funds	Low reliance on federal transfers	Prudent debt & liquidity management
	ESG consolidated impact	Applicable: Y/N	N	N	N	Y (Relevant)	N	Y (Relevant)	N	N	N	N
Fitch	Environment factors	Y/N	N	N	N	Y (Relevant)	N	Y (Relevant)	N	N	N	N
	Social factors	Y/N	N	N	N	N	N	N	N	N	N	N
	Governance factors	Y/N	N	N	N	N	N	N	N	N	N	N
	Date of rating report		12-Dec-25	10-Jun-25	9-May-25	18-Sep-25	20-Nov-25	21-Jan-26	14-Nov-25	4-Jun-25	18-Jul-25	8-Jul-25
	Long-term rating		AA-	AA-	AA+	AA	-	AA	-	-	-	-
	Outlook		Stable	Stable	Negative	Stable	-	Stable	-	-	-	-
	Short-term rating		F1+	F1+	F1+	F1+	-	F1+	-	-	-	-
	Stand-alone credit profile (SCP)		a+	a+	aa	aa-		aa-				
	Support (ad hoc, via federal govt)		+1 notch	+1 notch	+1 notch	+1 notch		+1 notch				
Fitch	Risk profile		Stronger	Stronger	Stronger	High Midrange		High Midrange				
	Revenue robustness		Stronger	Stronger	Stronger	Midrange		Midrange				
	Revenue adjustability		Stronger	Stronger	Stronger	Stronger		Stronger				
	Expenditure sustainability		Midrange	Midrange	Midrange	Midrange		Midrange				
	Expenditure adjustability		Stronger	Stronger	Stronger	Stronger		Stronger				
	Liability/liquidity robustness		Stronger	Stronger	Stronger	Stronger		Stronger				
	Liability/liquidity flexibility		Stronger	Stronger	Stronger	Stronger		Stronger				
	Debt sustainability category		'bbb'	'bbb'	'a'	'aa'		'aa'				
	ESG relevance score	1-5 (Low-High)	3 (Neutral)	3 (Neutral)	3 (Neutral)	4 (Negative)		3 (Neutral)				
Fitch	Date of rating report		20-Jun-25	20-Jun-25	5-May-25	4-Jun-25		4-Jun-25				
	Long-term rating		AA-	AA-	AA+	AA	-	AA	-	-	-	-
	Outlook		Stable	Stable	Negative	Stable	-	Stable	-	-	-	-
	Short-term rating		F1+	F1+	F1+	F1+	-	F1+	-	-	-	-
	Stand-alone credit profile (SCP)		a+	a+	aa	aa-		aa-				
	Support (ad hoc, via federal govt)		+1 notch	+1 notch	+1 notch	+1 notch		+1 notch				
	Risk profile		Stronger	Stronger	Stronger	High Midrange		High Midrange				
	Revenue robustness		Stronger	Stronger	Stronger	Midrange		Midrange				
	Revenue adjustability		Stronger	Stronger	Stronger	Stronger		Stronger				
Fitch	Expenditure sustainability		Midrange	Midrange	Midrange	Midrange		Midrange				
	Expenditure adjustability		Stronger	Stronger	Stronger	Stronger		Stronger				
	Liability/liquidity robustness		Stronger	Stronger	Stronger	Stronger		Stronger				
	Liability/liquidity flexibility		Stronger	Stronger	Stronger	Stronger		Stronger				
	Debt sustainability category		'bbb'	'bbb'	'a'	'aa'		'aa'				
	ESG relevance score	1-5 (Low-High)	3 (Neutral)	3 (Neutral)	3 (Neutral)	4 (Negative)		3 (Neutral)				
	Date of rating report		20-Jun-25	20-Jun-25	5-May-25	4-Jun-25		4-Jun-25				
	Long-term rating		AA-	AA-	AA+	AA	-	AA	-	-	-	-
	Outlook		Stable	Stable	Negative	Stable	-	Stable	-	-	-	-
	Short-term rating		F1+	F1+	F1+	F1+	-	F1+	-	-	-	-
Fitch	Stand-alone credit profile (SCP)		a+	a+	aa	aa-		aa-				
	Support (ad hoc, via federal govt)		+1 notch	+1 notch	+1 notch	+1 notch		+1 notch				
	Risk profile		Stronger	Stronger	Stronger	High Midrange		High Midrange				
	Revenue robustness		Stronger	Stronger	Stronger	Midrange		Midrange				
	Revenue adjustability		Stronger	Stronger	Stronger	Stronger		Stronger				
	Expenditure sustainability		Midrange	Midrange	Midrange	Midrange		Midrange				
	Expenditure adjustability		Stronger	Stronger	Stronger	Stronger		Stronger				
	Liability/liquidity robustness		Stronger	Stronger	Stronger	Stronger		Stronger				
	Liability/liquidity flexibility		Stronger	Stronger	Stronger	Stronger		Stronger				
Fitch	Debt sustainability category		'bbb'	'bbb'	'a'	'aa'		'aa'				
	ESG relevance score	1-5 (Low-High)	3 (Neutral)	3 (Neutral)	3 (Neutral)	4 (Negative)		3 (Neutral)				
	Date of rating report		20-Jun-25	20-Jun-25	5-May-25	4-Jun-25		4-Jun-25				
	Long-term rating		AA-	AA-	AA+	AA	-	AA	-	-	-	-
	Outlook		Stable	Stable	Negative	Stable	-	Stable	-	-	-	-
	Short-term rating		F1+	F1+	F1+	F1+	-	F1+	-	-	-	-
	Stand-alone credit profile (SCP)		a+	a+	aa	aa-		aa-				
	Support (ad hoc, via federal govt)		+1 notch	+1 notch	+1 notch	+1 notch		+1 notch				
	Risk profile		Stronger	Stronger	Stronger	High Midrange		High Midrange				
Fitch	Revenue robustness		Stronger	Stronger	Stronger	Midrange		Midrange				
	Revenue adjustability		Stronger	Stronger	Stronger	Stronger		Stronger				
	Expenditure sustainability		Midrange	Midrange	Midrange	Midrange		Midrange				
	Expenditure adjustability		Stronger	Stronger	Stronger	Stronger		Stronger				
	Liability/liquidity robustness		Stronger	Stronger	Stronger	Stronger		Stronger				
	Liability/liquidity flexibility		Stronger	Stronger	Stronger	Stronger		Stronger				
	Debt sustainability category		'bbb'	'bbb'	'a'	'aa'		'aa'				
	ESG relevance score	1-5 (Low-High)	3 (Neutral)	3 (Neutral)	3 (Neutral)	4 (Negative)		3 (Neutral)				
	Date of rating report		20-Jun-25	20-Jun-25	5-May-25	4-Jun-25		4-Jun-25				



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