Provincial Issuers Update:

Budget Preview & U.S. Tariffs Edition

Summary

Trade policy uncertainty induced by the new U.S. administration complicates budget planning for Canadian provinces and is expected to reduce Canadian real GDP growth from 1.7% to 1.2% in 2025; this poses significant challenges for provincial economies and budgetary balances.

Canadian provinces may need to issue up to $133 billion in bonds in FY 2025-26 if blanket 25% of U.S. tariffs are imposed on Canada; $121 billion under a 10% tariffs scenario on half of Canadian exports; and $113 billion without blanket tariffs.

Canada is the largest mining supplier to America. Several provincial governments have proactively launched a critical mineral strategy that could cushion Canada against sweeping U.S. tariffs.

Quebec: Investors and credit agencies are awaiting a credible plan in Budget 2025 to restore budgetary balance by FY 2029-30. U.S. trade policy uncertainty could delay this target, although Quebec's very diversified economy is a key pillar.

Ontario: Recent credit upgrades, and a sound fiscal situation tied to slower growth in expenditures put Ontario in a better financial position to handle U.S. tariffs.

British Columbia: There are growing signs of fiscal restraint in Budget 2025 in response to U.S. trade policy uncertainty contrasting with outsized deficits and credit downgrades of 2023 and 2024.

Alberta: The Trump administration's previous idea of relatively lower 10% tariffs on energy reveals the crucial importance of Canadian oil to the U.S., making Alberta less impacted compared to other provinces under a tariff shock scenario.

Saskatchewan would be less impacted by U.S. tariffs compared to most provinces, thanks to its diversity of export products and abundance of critical minerals.

Manitoba: The Manitoba government has launched a critical mineral strategy to expedite projects and partnerships with First Nations, on top of facing a large budget deficit and average exposure to U.S. tariffs.

Newfoundland & Labrador is potentially exposed to a lower effective tariff shock than most. The government preparing for an electoral budget will have to decide how to allocate the revenue windfall from the new Churchill Falls deal.

New Brunswick's small business confidence has been declining due to higher reliance on U.S. exports, while the new provincial Liberal government inherited a moderate deficit.

Nova Scotia's Budget 2025 released in mid-February contains significant tax relief and increased spending, resulting in a larger-than-usual deficit and a rising net debt-to-NGDP ratio.

Context

The new U.S. administration complicates the budget planning process of Canadian provincial governments. Market participants will put more than usual attention to fiscal sensitivities, particularly the implications of an alternative tariff scenario—most likely 25% of U.S. tariffs on Canada and Mexico—on the budgetary balance, debt figures, and bond issuance.

It will be interesting to see if provincial governments incorporate in their budgets deferred spending from businesses and households caused by the current trade policy uncertainty into their baseline scenario. Models suggest such uncertainty could reduce Canadian economic growth by approximately half a percent this year. This represents a manageable adverse shock for provincial governments. Our economic team revised down Canadian real GDP growth forecast from 1.7% to 1.2% in 2025.

But since U.S. President Trump leans in favour of using tariffs to generate new tax revenues in the long run — not only as a short-term negotiation tactic to gain non-economic concessions — the paths of real GDP and fiscal revenue beyond 2025 could have to be trimmed too. Thus, governments controlling and adjusting spending quickly will be able to show manageable budgetary balances, or alternatively accept a structural deterioration in public finances.

Canadian provinces issued $139 billion in FY 2024-25 as of the third week of February, or $125 billion considering the $14 billion in pre-financing activity for FY 2025-26. Our tracking of previous fiscal updates and budgets would have pointed to $108 billion in bond issuance during FY 2025-26. However, the slower economic growth path induced by U.S. trade policy uncertainty implies a combined provincial issuance of at least $113 billion. Provinces could tap markets for $121 billion under the assumption of 10% tariffs on half of Canadian exports, excluding energy and auto manufacturing. In the case of 25% sweeping tariffs, our estimate goes up to $133 billion, shy of the pandemic peak of $160 billion, even if governments have signalled their intention to provide financial support during the tariff shock.

Quebec, Ontario, BC, Saskatchewan, PEI, and NB have pre-financing activity totalling $14 billion for FY 2025-26 as of the third week of February, benefiting from receptive market conditions before the serious threat of U.S. tariffs started to complicate things. Provinces issued a larger-than-usual 38% of bonds outside of Canada during FY 2024-25. Such a repeat appears unlikely in FY 2025-26 if Canada continues to be overly exposed to U.S. tariff threats relative to other developed countries, which could put pressure on the domestic bond market.

Canada sold $30 billion of critical minerals to the U.S. in 2023, according to Natural Resources Canada, making Canada the largest mining supplier to America. The U.S. plans to reduce its reliance on China and thus needs additional Canadian critical minerals for its energy transition, defence industry, and to race ahead of China on AI. Ottawa has already indicated it could take additional non-tariff measures affecting critical minerals, one way for provinces to expand this industry and cushion Canada against long-term punitive U.S. tariffs. The latest IEA Critical Minerals Outlook cites that Canada has the potential to expand critical mining production despite lags in processing facilities.

Quebec – Could U.S. Tariffs Delay the Return to a Balanced Budget?

In the summer edition of the Provincial Issuers Update, we highlighted the patience of investors and credit agencies waiting to see a credible plan in Budget 2025 restoring budgetary balance by FY 2029-30. Quebec has the fiscal capacity to achieve such a turnaround despite the unusually large FY 2024-25 deficit of $11 billion. Indeed, the Fall fiscal update emphasized on the 277 fiscal expenditures costing the government $40 billion per year. We expect some of these fiscal expenditures, which include several refundable tax credits granted to individuals and businesses, to be abolished or gradually phased out in Budget 2025.

While this looks promising on paper, the harsh reality of U.S. trade policy uncertainty must be considered. If Budget 2025 prudently incorporates a weaker revenue path due to U.S. tariffs hindering business and consumer spending, the question becomes: “to what extent can the Quebec government raise additional taxation rates and/or cut spending as a percentage of nominal GDP to sufficiently narrow the deficit and still target a return to balance in FY 2029-30?”

The alternative “recession scenario” illustrated in the fall fiscal update provides valuable insights into what may happen next (even though a classic cyclical recession shock differs from a tariff shock). Under a mild 0.3% contraction of Quebec’s real GDP in 2025, the FY 2026-27 deficit is pegged at $11 billion, or $2 billion more than under the base case scenario. Thus, under a tariff shock, it could be a challenge for the Quebec government to keep annual borrowing requirements slightly under $30 billion in FY 2026-27 as originally planned in the fall fiscal update.

The Quebec economy has one of the most diversified export sectors in North America, according to the Herfindahl-Hirschman index of 0.05 (under 0.15 is considered a diversified product market; between 0.15 and 0.25 is considered moderately concentrated exports in either product and/or destination.). Accordingly, Quebec can cope at the macroeconomic level with the possibility of 25% tariffs on aluminum becoming effective in March. Also, the Quebec government has been ahead of the curve in respect to the development of critical minerals with a strategy in place since 2020.

Ontario – Sound Financial Position to Face Tariff Uncertainty and Planned U.S. Tariffs on Steel

Over the years, the pace of expense growth by the Ontario government has been materially lower than Quebec and BC. Following the DBRS credit upgrade from AA- to AA in June 2024, the S&P agency also upgraded Ontario’s long-term rating from A+ to AA- in December. Ontario managed to move close to a balanced budget position before U.S. trade policy uncertainty soared. As such, Canada’s largest province will have more fiscal flexibility to cushion the blow in case of an adverse tariff shock. Key actors in the North American auto industry reacted strongly to the possibility of sweeping tariffs on Mexico and Canada. The Ford CEO stated that tariffs would be a blow to the industry, while the GM CEO mentioned a contingency plan including a possible shift in assembly and parts in case of persistent tariffs. Reports such as S&P Global Mobility indicate that tariffs would add about U.S.$6K to the price of a car imported from Mexico and Canada. It remains unclear if the mid-February idea from U.S. President Trump of imposing 25% tariffs on automobile imports primarily targets Europe or includes Canada. The planned 25% U.S. tariffs on Canadian steel in March will disproportionately impact Ontario, home to almost half of Canada’s steel manufacturers.

If U.S. tariffs become widespread on most exports, the sensitivities provided in the Ontario Fall Economic Statement offer a good reference to assess the potential fiscal impact. The "slower" growth scenario, incorporating a mild 0.3% real GDP expansion in 2025, points to annual borrowing requirements of $42 billion in FY 2025-26, versus $35 billion in the base-case scenario. If a U.S. tariff shock becomes reality and lasts for at least six months, Ontario's real GDP would likely contract. Under such circumstances, the province could use some of its above historical-average liquidity reserve of $43.4 billion to stabilize annual bond issuance and prevent it from surpassing $45 billion.

British Columbia – The Return of Manageable Deficits in Budget 2025?

Prior 2023 and 2024 budgets revealed large deficits with no end in sight, contributing to credit downgrades in both years. The 2025 BC budget, to be released on March 4th, could introduce fiscal restraint. The new Finance Minister, Brenda Bailey, was appointed in November following a nail-biting election race that resulted in the NDP retaining its majority status. Previous Finance Minister Katrine Convoy was the first last fall to express the idea of presenting a balanced budget plan. Such a proposal appears a steep hill to climb given the FY 2024-25 deficit of $9.4B and trade policy uncertainty. A more realistic option is to show manageable deficits over three years in Budget 2025. Such a signal would be a major game changer given the current mainstream market view that BC is on track to issue a lot of bonds in the years ahead. Tilting toward fiscal restraint would reduce the risk of another credit downgrade. Moody's and S&P credit agencies both have a negative watch on BC's long-term outlook. Minister Bailey indirectly alluded to a shift toward fiscal restraint in mid-December when she delivered the mid-year update, referring to a more challenging environment for revenues tied to lower commodity prices and higher interest rates. Then, in mid-February, the BC government confirmed the cancellation of a $1,000 grocery rebate promised during the election campaign, a measure that was not incorporated in the fiscal outlook and that would have cost $2B. A hiring freeze of public sector workers has also been announced.

One rare certainty BC holds is that the first exports of LNG are on track for mid-2025. Fourteen million tonnes of LNG per annum from the LNG Canada site will significantly boost BC's real GDP. However, the impact on fiscal finances has already been incorporated into Budget 2024. Annual natural gas revenues are projected to approximately double over two years, from $600 million in FY 2024-25 to $1.4 billion in 2027. In January, the BC government released its preliminary assessment of 25% tariffs, including a 0.6 percentage point reduction relative to the baseline scenario for real GDP growth in both 2025 and 2026. There is a case to be made that BC would be relatively less adversely affected by U.S. tariffs in Canada than Ontario and Quebec, given its lower U.S. market share exposure. The largest U.S. tariff shock so far concerns China, indirectly impacting BC more than any other Canadian province due to its ties with Asia. However, stimulus efforts from Chinese authorities to foster growth, observable thru the money supply surge of late 2024, should contribute to offset the tariff shock.

Finally, another advantage for BC relates to its solid positioning in respect to critical minerals, as highlighted by a map from Natural Resources Canada. BC is ahead of several provinces, having launched the first phase of the Critical Minerals Strategy a year ago. Among flagship critical mining, BC is home to almost half of Canada's copper production.

Alberta – Subject to a Lower Effective Tariff Rate Than Peers

Given the exposed threat of imposing 25% tariffs on non-energy products from Canada, and 10% on energy, the Trump administration has acknowledged the crucial importance of Canadian oil to America. As reported by the U.S. Energy Information Administration, crude oil imports from Canada have become vital to U.S. oil refineries, particularly in the Midwest PADD II region. The U.S. plans to reduce the small oil imports from Venezuela, which produces a similar heavy crude to Western Canadian Select (WCS). Additionally, while President Trump's "Drill, Baby, Drill" rhetoric resonates, the reality on the ground seems unimpressive. OPEC forecasts a mild 2.3% increase in U.S. oil production this year, while the EIA projects 3.5%. In both cases, such increases cannot replace Canadian oil. Under a realistic scenario of higher tariff rates on non-oil U.S. imports (25%) compared to U.S. energy imports (10%), Alberta's all-in effective tariff rate would be materially lower, closer to 15%, relative to other Canadian provinces facing an effective tariff rate ranging between 20%-25%. Consequently, Alberta's real GDP, nominal GDP, and fiscal revenue growth would slow less than other Canadian provinces, even though some crucial sectors, such as agriculture, would face 25% tariffs.

Global oil markets may appropriately disregard the tariff threat on Canadian oil. Evidence lies in the very small WTI-WCS (light heavy) differential of U.S.$11 per barrel. This small discount stands below the assumption used in the mid-year fiscal update (U.S.$14.60, on average, in FY 2024-25 and FY 2025-26). This WTI-WCS spread narrowed compared to a year ago due to the Trans Mountain pipeline sending Alberta's oil production to record highs. However, WTI price levels have recently traded below the assumption used in the mid-year update (U.S.$75 per barrel in calendar 2025). Meanwhile, the Canadian dollar has been trading softer than expected. Overall, we do not foresee any fundamental changes in Alberta's fiscal performance in Budget 2025, although recent developments could point to a slight downward revision to the mid-year update FY 2024-25 surplus estimate of $4.6 billion.

Besides President Trump's tariffs, another element for markets to consider is the unusually large amount of Alberta bonds maturing in FY 2025-26, close to $13.2 billion. This compares to approximately $6 billion in both FY 2024-25 and FY 2026-27. $10.9 billion of debt will mature between April and June 2025. The Alberta government holds a good liquidity buffer, near $3 billion.

Finally, Alberta's role in critical minerals is set to expand. According to the Alberta Energy Regulator, lithium production will begin in 2026 and soar by 2028. The province's Minerals Strategy details a list of 13 critical minerals and existing refineries.

Saskatchewan – U.S. Export Concentration, but Rich in Critical Minerals

Proposed tariffs would impact Saskatchewan less than most provinces, except for Newfoundland and Labrador (N&L) and Alberta, which have a higher percentage of GDP tied to oil.

The concentration ratio of export products in Saskatchewan is relatively higher than the Canadian average, according to the Herfindahl-Hirschman index, as the province ships heavily to America. In terms of products, there are silver linings. Saskatchewan is notably home to 27 of the 34 critical minerals identified by the federal government. One flagship mineral is potash. The world's largest potash mine, located in Saskatchewan, is expected to start its production phase in 2026. Additionally, in our energy report on nuclear energy, we purposely stop short of referring to raw uranium ore, the only fuel supplied for nuclear reactors. Given the pivotal role of nuclear energy in meeting growing U.S. energy requirements, uranium is less likely to be subject to U.S. tariffs.

Overall, Saskatchewan's broad financial picture looks better than recent short-term results. The hot and dry month of July 2024 weighed down on crop production and contributed to increased agriculture expenses for the Saskatchewan government beyond budget expectations. This temporary factor contributed to the worsening of the FY 2024-25 deficit, now projected at $744 million in the Mid-year update instead of $470 million in Budget 2024. Budget 2025 will be released on March 14th.

Manitoba – One of Many Provinces Rich in Critical Minerals

The Manitoba government has released its Critical Mineral Future strategy in November to speed up projects and facilitate partnerships with First Nations. The province is home to 30 of 34 critical minerals identified by the federal government. Last year, additional in-depth geophysical surveys to unlock additional nickel supply has been done at the Thompson site. Manitoba's first potash mine also opened last summer.

During his mid-February trip to Washington, DC with other Canadian Premiers, Manitoba Premier Wab Kinew referred to the multiple cross-border of manufacturing and agriculture products in his province. As such, Manitoba is not an outlier in terms of exposure to U.S. tariffs relative to the Canadian average. A tariff shock would further deteriorate public finances. Already, the 2nd quarter report of last December indicated a large $1.3 billion deficit in FY 2024-25, up from $0.8 billion in Budget 2024.

Newfoundland and Labrador – Lower Tariff Exposure, Elections in 2025

The oil and gas industry accounts for a quarter of the province's GDP. The lower likelihood of sweeping U.S. tariffs on Canadian oil would place N&L in a relatively less disadvantageous position under a trade war scenario. First, N&L, along with Alberta, is the only province where oil exports surpass non-oil exports. Second, N&L exports more oil to Europe than to the U.S.

As mentioned in our report on hydro and wind power evolution, the new Memorandum of Understanding on Churchill Falls between N&L and Quebec will notably bring an extra $1 billion annually until 2041. Premier Andrew Furey stated in mid-December that part of this new recurrent revenue stream could be allocated to debt reduction. N&L has a net debt of $18 billion and market borrowings of $19 billion, a substantial burden considering the population of 546,000. The exact distribution between debt reduction, operational spending, and capital spending will be one of the key features to watch for in Budget 2025. Budget 2025 will be an electoral budget, as a general election will take place on or before November 24.

The mid-year update of last October showed a manageable FY 2024-25 deficit of $218 million. Since then, there have been no material developments. Brent oil has been trading below the U.S.$81 per barrel assumption, but the CAD/USD exchange rate has been weaker than the 73.2 cents assumption.

New Brunswick – New Government Begins Term with a Moderate Deficit in Hand

Small business confidence deteriorated to a greater extent in New Brunswick in late 2024 and early 2025 than in other provinces, according to the Canadian Federation of Independent Businesses. This is unsurprising given NB's higher reliance on U.S. exports, measured by the elevated Herfindahl-Hirschman Index. Tariff-induced uncertainty is problematic for the NB Liberal Party poised to deliver its first budget following the majority win in the October general elections. The previous PC government had registered huge surpluses in recent years and materially reduced the net debt-to-NGDP ratio below 30%.

Higher health care spending associated with funding for nurses, a sales tax rebate on electricity bills, and the temporary GST/HST break contributed mostly to the deterioration in public finances recently. The third-quarter fiscal update unveiled a $399 million deficit in FY 2024-25. Such a sizeable shortfall makes a balanced budget in Budget 2025 a near-impossible task given the heightened U.S. tariff policy uncertainty.

Nova Scotia – From a Streak of Surpluses to Deficit Territory

Nova Scotia was the first province to release Budget 2025, on February 18th. It marked the first PC budget since its re-election last November. The PC government incorporated substantial tax relief in Budget 2025. First, a 1% reduction in the HST will become effective in April. Second, a $200,000 increase in the income threshold necessary to be eligible for the small business corporate income tax rate of 2.5% will also become effective in April. Both measures will result in total flat revenues during FY 2025-26 relative to the previous year. Combined with a higher-than-usual 6% annual increase in total spending, Budget 2025 pegs the deficit at $900 million, a relatively large amount contrasting with small surpluses registered the previous four years. Budget 2025 includes an annual contingency of $200 million of the 4-year fiscal plan due to U.S. tariff uncertainty, a reasonable amount representing 1.2% of total revenues. Real GDP annual growth forecasts underpinning the revenue outlook, 2% in 2025 and 1.8% in 2026, appear optimistic but reflect the stimulus impact of tax cuts and additional funding to capital spending.

The government intends to gradually reduce the deficit to zero over four years if the $200 million annual contingency is untapped. The switch from surpluses to deficits materially changes the course of the net debt-to-NGDP ratio. The latter is on a steeper uptrend, from 34.6% in FY 2024-25 to a projected 40.9% in FY 2028-29. Altogether, projected borrowing requirements are unambiguously higher than in Budget 2024, including $3.2 billion in FY 2025-26 versus $2.531 billion for FY 2024-25. Finally, there has been a higher-than-usual increase in the average term to maturity, rising by 1.1 years to 15.5 years over the last year. The province successfully launched a 50-year bond, re-opened its previous 30-year benchmark, and issued a new 30-year debenture over the course of FY 2024-25.

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