

March 20, 2024

Staying in deficit & adding debt to finance record investments

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Highlights

Lower-than-expected commodity prices, drought, and increased pressure on public services due to record population growth have significantly changed the province's financial picture as presented in the 2023 budget, with the \$1.02 billion surplus for the outgoing fiscal year turning into a \$482.5 million deficit. Faced with less buoyant economic growth due to the restrictive interest rate environment, the 2024 Budget forecasts a smaller deficit of \$273.2 million for the fiscal year 2024-25, due to a contraction in spending greater than that of revenues, before returning to surplus territory in 2025-26 and subsequent years. Despite the contraction in spending, the budget dubbed 'Classrooms, Care & Communities' focuses on the state's core missions, with record spending on education and health, plus a significant increase in municipal revenue sharing. Despite an enviable fiscal position relative to other Canadian provinces, with the second-lowest net debt-to-GDP ratio in Confederation (after Alberta), two years of deficit, a couple of years of budgetary deficits (in 2023-24 and 2024-25), alongside sizeable strategic capital investments, has net debt on an upward trajectory. As a result, the net debt-to-GDP ratio is expected to increase from 13.3% to 14.0% at the end of the 2024-25 fiscal year and to reach 14.6% in 2025-26/2026-27. Finally, Budget 2024 outlines a non-trivial increase in gross borrowing requirements to \$4.36 billion compared to \$2.7 billion in the outgoing fiscal year.

- **Economic outlook** – After being the Canadian province with the strongest real GDP growth at 6.0% in 2022, the pace of economic growth in Saskatchewan is estimated to be much more modest in 2023 at 1.4% but remained higher than that observed for the country as a whole (+1.1%). This less vigorous growth can be explained notably by the growing impact of restrictive monetary policy on the economy, despite an historical population growth of 2.6% in 2023. As for nominal GDP, which has a greater influence on public finances, it is estimated to have contracted slightly by 0.3%, undermined by a reduction in commodity prices, particularly potash. Regarding the labour market, employment growth in the province was just 1.8% in 2023 (Canada: +2.4%), despite record population growth. As a result, the unemployment rate has risen from 4.5% in February 2023 to 5.0% in February 2024, but remains the third lowest in the Confederation. Looking ahead, the Budget is based on the average private-sector forecast. Real GDP growth in 2024 should continue to moderate to 1.0%, before reaching 1.8% in 2025, 2.3% in 2026, 2.1% in 2027, and 2.2% in 2028. As for nominal GDP, it is set to pick up again in 2024, helped by a stabilization in commodity prices, and to grow by 2.1%. It should then rise by 3.2% in 2025, 3.7% in 2026, 3.5% in 2027 and 4.1% in 2028. Regarding the labour market, employment growth should also moderate in 2024, pushing the unemployment rate up to 5.5% on average for the year. The unemployment rate should then peak at 5.6% in 2025 and 2026, before falling back marginally to 5.5% in 2027 and 2028.
- **Outgoing year budget balance (2023-24)** – The third official update to fiscal 2023-24 marks a third straight downgrade for Saskatchewan's budget balance. The \$1 billion surplus (0.9% of GDP) originally planned in last year's budget was watered down to just under \$500 million in a Q1 update, revised to a \$250 million deficit in the mid-year update and is today, further downgraded to a \$483 million shortfall (0.4% of GDP). The deterioration wasn't a function of softer revenues. In fact, the province brought in \$705 million more than budgeted (+3.6%) thanks to material beats on all revenue components except for non-renewable resources. It's worth noting that the miss on non-renewable revenue was substantial. Proceeds are expected to come in roughly \$950 million (or nearly 30%) below plan. In any event, it was really the \$2.2 billion (+11%) jump in spending that drove the budgetary deterioration. Half of that is a function of the agriculture sector and the impact of droughts that plagued parts of the province. Operational pressures in the health sector saw spending in this sector come in \$488 million higher than planned, while marginal education expenses made up \$254 million of spending miss.
- **Medium-term fiscal outlook (2024-25 & beyond)** – Saskatchewan's fiscal situation is set to improve in 2024-25 but the small surplus that was previously signalled won't be in the cards. Instead, the province is guiding us to a modest \$273 million deficit (0.2% of GDP). As noted above, significant unplanned agriculture spending drove this outgoing year's deterioration. The roughly \$1 billion reduction in that envelope next year will therefore help bring down overall spending by 3.5%. Not surprisingly though, expenses will be up elsewhere. The province sees spending on health rising 1.3%, education climbing 2.9% and social services jumping 4%. On the revenue side, Saskatchewan expects moderation too. Total receipts are set to drop 2.6% with that being primarily driven by a decline in tax revenues (which itself can be attributed to a slowing economy). Meanwhile, after below-budget receipts in 2023-24, the government is planning for a healthy 12.2% bounce back in non-renewable resource revenue, which accounts for 13.5% of total inflows. The budget cites a tighter light-heavy differential as the main driver here. After the small 2024-25 deficit, an updated fiscal plan sees the province returning to balance in 2025-26 (officially an \$18 million surplus). The expected surplus is then seen as growing to \$225 million (0.2% of GDP) in 2026-27 and then to \$340 million (0.3% of GDP) in 2027-28. In these three outer years of the fiscal plan, revenue is expected to grow at an average annual rate of 3.8% and spending growth is seen expanding at a relatively well contained 2.8%/year.
- **Energy price assumptions & related sensitivities** – When it comes to planning assumptions, the budget assumes WTI will average US\$77/bbl during fiscal 2024-25. On budget day, the front WTI contract was trading at roughly US\$82 which the province will hope

holds up. Medium-term thinking sees WTI hovering between US\$75-79/bbl through 2028. As for the light-heavy oil price differential, it is expected to average 14.5% of WTI in 2024-25. That gap currently hovers around there today. The budget notes that the tighter differential (relative to last year) is driven by a decrease in availability of heavy crude types from other suppliers and improved pipeline capacity. Official sensitivities imply each US\$1/bbl change in WTI is worth \$17.5 million in revenue to the province, all else equal. Meanwhile, oil production is forecast to come in at 167 million barrels, a level unchanged from the outgoing fiscal year. Elsewhere, potash is assumed to average US\$268/KCl tonne in the coming fiscal year. That's down a bit from the US\$284 averaged in the outgoing fiscal year and is well below the US\$369 that was originally budgeted for 2023-24. Finally, the budget expects the Canadian dollar to average 74.36 US cents in 2024-25, with each US cent worth \$36 million in resource revenue.

- **New measures** – Dubbed 'Classrooms, Care & Communities', the priorities of the 2024 Budget are clear. On the education front, the budget allocates an additional \$125 million, an increase of 2.9% on the previous year, bringing education spending to a record \$4.4 billion. These additional sums will be used notably to finance direct classroom supports (including funding to address classroom size and complexity), prekindergarten to grade 12 schools, early learning, child care, libraries and post-secondary education. On the care front, the budget outlined a record health care spend for 2024-25 (\$7.64 billion or some 38% of total expenses). Health care is the largest line item in the budget and is up \$96 million or 1.3% from last year. Among other initiatives, the plan has allocated additional funding for breast cancer care and screening, the Saskatchewan Cancer Agency to increase volumes and access to the most advanced treatments, the Health Human Resource Action Plan to add 250 new or enhanced permanent positions in rural and remote locations, and the Saskatoon and Regina Capacity Pressures Action Plan to enhance acute care, community-based care and emergency department capacity. Finally, on the communities' front, the budget increases the municipal revenue sharing compared to 2023 budget by \$42.4 million to \$340 million.
- **Debt burden & interest bite** – A couple of years of budgetary deficits (in 2023-24 and 2024-25), alongside sizeable strategic capital investments, has net debt on an upward trajectory... admittedly from a relatively low starting point. For the coming fiscal year, \$1.18 billion of net debt is slated to be tacked on, with the clear majority traced to the acquisition of tangible capital assets. At \$16.35 billion, the projected level of net debt forecast as of March 2025 would be equivalent to 14.0% of GDP, this relative leverage metric rising for a second straight fiscal year. As per the fresh medium-term outlook, debt-to-GDP is seen topping out at 14.6% in 2025-26/2026-27. Notwithstanding the rising debt load, Saskatchewan's debt burden would remain below the pandemic-related peak (17.5%) and would also continue to reside at the lower end of the provincial spectrum. (Only Alberta has a lower debt ratio. Looked at another way, the 14% debt burden in Saskatchewan would be less than half the provincial average, which we see surpassing 30% in 2024-25 on a weighted average basis.) As in other jurisdictions, higher interest rates mean financing charges on the rise. In Saskatchewan's case, a double-digit percentage increase would see financing charges consuming a comparatively modest/manageable 4.6% of total revenue in 2024-25. Again, that's relatively low by provincial standards. (This version of the 'interest bite' was equivalent to 4.0% in 2023-24.)
- **Borrowing requirements** – As in a few other corners of the provincial market, Saskatchewan expects to be a more active issuer. But first a word on the outgoing, 2024-24 fiscal year. With less cash available to fund the capital plan, total borrowing requirements pushed roughly \$1 billion above the Budget 2023 target. Setting aside internal financing sources and incremental short-term financing, that resulted in \$2.26 billion in long-term borrowing in 2023-24 (vs. the \$1.17 billion originally planned for). Completed financings were exclusively domestic, including the regular supply of 10- and 30-year benchmark bonds alongside some ultra-long issuance (currently out to 2062). Turning to 2024-25, Budget 2024 outlines a non-trivial increase in gross borrowing requirements to \$4.36 billion. Again, this is primarily a function of capital needs plus on-lending for Crowns. The borrowing strategy identifies \$380 million to be sourced from short-term markets leaving just under \$4 billion in long-term financing for the coming 12 months. Based on our records, that would be more-or-less in line with the amount of marketable bond issuance Saskatchewan brought at the peak of the pandemic in 2020-21. While a relatively large program by this province's standards, the projected bond program—when expressed in per capita terms or scaled to revenue—would land somewhere in the middle of the range so far telegraphed via other 2024 provincial budgets. Overall, you could see this as part of a movement to larger funding requirements for the provincial sector as a whole, with Saskatchewan notably situated at the higher end of the credit rating spectrum. Notwithstanding prospective capital plan and Crown needs further down the road, an expectation of a return to balance from 2025-26 onwards and generally contained refinancing requirements (linked to the lower debt burden) hint at manageable bond issuance over the medium-term.
- **Current long-term credit ratings** – S&P: AA, Stable | Moody's: Aa1, Stable | DBRS: AA(Low), Stable | Fitch: AA, Stable
[Refer to our Provincial Ratings Snapshot for additional colour on specific credit rating drivers/considerations]

Saskatchewan

\$000 000

Consolidated Budget

	Budget	Forecast	Budget	Plan		
	2023-24	2023-24	2024-25	2025-26	2026-27	2027-28
Total revenues	19,677.7	20,383.2	19,861.9	20,617	21,400	22,213
Taxes	9,633.8	10,270.4	9,723.3			
of which provincial sales tax	2,720.3	2,894.2	3,196.4			
Non-renewable resources	3,344.6	2,393.4	2,686.3			
Net income from Government Business Enterprises	529.1	800.7	657.0			
Other revenue	2,615.6	3,183.6	3,015.6			
Transfers from the Government of Canada	3,554.6	3,735.1	3,779.7			
Total spending	18,660.2	20,865.7	20,135.1	20,598	21,175	21,874
Program expenditure	17,848.0	20,041.3	19,223.6			
As of Health	7,056.3	7,543.8	7,639.8			
As of Education	4,035.7	4,289.6	4,414.5			
As of Other	6,756.0	8,207.9	7,169.3			
Debt servicing	812.2	824.4	911.5			
Surplus (deficit)	1,017.5	(482.5)	(273.2)	18.5	225.1	339.6

Public debt (end of year - net of sinking funds)

General Revenue Fund and Gov. Service organizations	18,083.8	19,184.5	21,063.1
Government Business Enterprises	12,771.5	12,613.8	13,749.4
Total: Public Debt	30,855.3	31,798.3	34,812.5

Net Debt

Beginning of year	14,967.6	14,597.8	15,168.8	16,347.3		
Summary deficit (surplus)	(1,017.5)	482.5	273.2	(18.5)	(225.1)	(339.6)
Acquisition of Government Service Organization Capital Assets	1,341.6	1,279.1	1,597.1			
Amorization, disposal and adjustments	(1,163.6)	(1,190.6)	(691.8)			
End of year	14,128.1	15,168.8	16,347.3			
As a % of GDP	13.2%	13.3%	14.0%	14.6%	14.6%	14.3%

Borrowing requirements

Borrowing requirements	1,675.6	2,677.9	4,364.0
Government Service Organizations	600.0	1,700.0	2,827.4
Government Business Enterprises	1,075.6	977.9	1,536.6

Pension liabilities

Beginning of year	6,113.0	6,119.0	6,110.4
Adjustment to account for pension costs on an accrual basis	(290.9)	(8.6)	(135.4)
End of year	5,822.1	6,110.4	5,975.0

Source: Budget documents, Saskatchewan Ministry of Finance.

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