S&P Global Ratings

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Research Update:

Province of Alberta Long-Term Issuer Rating Raised To 'A+' From 'A' On Significantly Lower Deficits; Outlook Stable

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Overview

- We believe that Alberta would be able to sustain a stronger budgetary performance and gradual decline in tax-supported debt burden over the next few years, even considering structural fiscal volatility due to the province's exposure to changes in oil prices.
- The strong economic recovery and the surge in the price of oil that began in 2021 led to significantly stronger budgetary results; we estimate that Alberta's operating deficits will average 2% of operating revenue and deficits after capital expenditures should remain below 11% of total revenues in 2020-2021 – 2024-2025.
- Accordingly, we raised our long-term issuer credit rating on the Province of Alberta and our issue-level rating on the province's senior unsecured debt to 'A+' from 'A'. At the same time, we affirmed our short-term rating on the province at 'A-1'.
- The stable outlook reflects our expectation that robust economic growth during the next two years will lead to continuing improvement in Alberta's budgetary performance and limit increases in the province's tax-supported debt burden.

Rating Action

On May 19, 2022, S&P Global Ratings raised its long-term issuer credit and senior unsecured debt ratings on the Province of Alberta to 'A+' from 'A'. At the same time, S&P Global Ratings affirmed its 'A-1' short-term rating on the province. The outlook is stable.

Outlook

The stable outlook reflects our expectation that Alberta's budgetary performance will remain stronger than in the past years, as a result of robust economic growth and high oil prices. We expect that a prudent financial planning will keep after-capital deficits smaller while the province's tax-supported debt burden will likely remain below 200% in 2022-2023. In addition, we expect shrinking after-capital deficits should lead to strengthening debt service coverage.

Downside scenario

Over the next two years, a return to consistently weak economic performance and large and persistent after-capital balances, coupled with the absence of timely policy responses to restore fiscal sustainability, could lead us to revise the outlook to negative or lower the ratings.

Upside scenario

Continuing economic and operating revenue growth in the next two years, coupled with the buttressing of the province's progress on increasing fiscal sustainability against the potential for declining oil prices could lead us to revise the outlook or raise the ratings. In this scenario, we expect that average after-capital balances would improve, reaching balance or near-balance on a consistent basis and that the province's debt burden would steadily decline.

Rationale

The upgrade reflects the strong economic recovery as well as the rebound in oil prices that have led to a significant improvement in the province's budgetary balances. Operating revenues increased more than 40% in fiscal 2021-2022 and we expect they will increase about 6% in our base-case scenario for fiscal 2022-2023. The province's operating balances have returned to positive territory from an operating deficit of more than 30% of operating revenues in fiscal 2020-2021. After-capital deficits have improved in tandem and the tax-supported debt burden has fallen. Our base-case scenario indicates that the province will continue to show operating surpluses and manageable deficits after capital expenditures in 2022-2023 – 2024-2025. Tax supported debt is likely to remain below 200% of operating revenues in the same period. We now believe the province's key quantitative and qualitative credit factors will remain reflective of the 'A+' rating.

The recovery in the Canadian economy and in oil prices has brought economic and fiscal relief to Alberta. S&P Global Economics' current baseline assumption is that Canada's real GDP will expand a further 3.7% in 2022 following a 4.6% rebound in 2021 (see "Economic Outlook Canada Q2 2022: Growth Forecasts Hold Up As Global Risks Rise," published March 28, 2022, on RatingsDirect). The province estimates that its real GDP rebounded by 5.8% in 2021 and this will be followed by a 5.4% expansion in 2022, outpacing the national averages in both years.

The prospects for the province's oil industry improved significantly in 2021 and has continued into 2022. On April 28, 2022, we raised our price assumptions for West Texas Intermediate (WTI) for the remainder of 2022 and 2023 (see "S&P Global Ratings Raises Oil And Gas Price Assumptions On Persistent Geopolitical And Supply Concerns," April 28, 2022). We expect WTI prices will now average US$85 per barrel (/bbl) for the remainder of 2022, US$70/bbl for 2023, and US$50/bbl for 2024 and beyond. The province's oil price assumptions are more conservative than S&P Global Ratings' for 2022, identical for 2023, and more optimistic for 2024. Accordingly, we have adjusted the province's revenues to account for these differences.

Operating balances have improved dramatically as oil prices have climbed and the pandemic has receded; after-capital results echoed the improvement

Almost all pandemic-related restrictions in Alberta were lifted earlier this year as almost 90% of Albertans became fully vaccinated and the coronavirus receded. Oil prices have risen significantly in the past year on supportive demand-supply conditions. Provincial revenues jumped in fiscal 2021-2022 and will increase modestly again in fiscal 2022-2023. Operating balances strengthened in tandem: The operating surplus represented 0.4% of operating revenues in 2021-2022 and we expect it will improve further to almost 10%. in 2022-2023After-capital balances followed the same path, improving to 8% of total revenues in 2021-2022 and are expected to turn to a 2% surplus in 2022-2023.

Budgetary performance will remain stronger in 2022-2023 – 2024-2025. Our base-case scenario indicates that operating and after-capital deficits will average 2.0% and 11.3% of operating and total revenues deficit for 2020-2021–2024-2025, respectively. This is a significant improvement from past years, when Alberta's financial performances was significantly weaker than that of peers.

With the substantial increase in operating revenues, Alberta's tax-supported debt burden is expected to decrease in relation to the province's operating revenues. We estimate that tax-supported debt will reach almost C$120 billion or about 200% of operating revenues by the end of 2024-2025. Our calculation of tax-supported debt includes guarantees and obligations under public-private partnership agreements. Interest expense will track lower as well: It will average 4.2% of operating revenues for fiscal 2021-2022–2023-2024. We continue to view the province's contingent liabilities as neutral to our debt assessment. The largest contingent liability is for ATB Financial, a local financial institution wholly owned by Alberta, to whose depositors the province provides a guarantee. As well, we consider the provincial credit union sector to be is a contingent liability, as the regulation of the sector is a provincial responsibility. Total contingent liabilities are modest, representing about 11% of fiscal 2022-2023 operating revenues.

Alberta's liquidity position is strong given the access to external liquidity. Also, Alberta's recent declining after-capital deficits are buoying the province's near-term internal liquidity, which had weakened with the deteriorating budgetary results in the past. We estimate that the province's free cash and investment balances will represent more than 76% of the next 12 months of debt service. We estimate free cash balances and investments will be about C$25 billion in the next 12 months. Alberta's access to external liquidity remains strong as demonstrated by its large market presence and access to Canada's well-developed capital markets.

Despite potential headwinds, the provincial economy will continue to expand at a healthy pace in 2022 while financial management remains prudent

The provincial economy will expand in 2022 as the pandemic recedes and the effects of high oil prices spread across other sectors. Alberta expects real GDP will increase 5.4% in 2022, following a 5.8% expansion in 2021. We expect that provincial real GDP growth of 3.5% will outpace the national average again in 2023, as it did in the past two years. The unemployment rate is forecast to fall to 6.6% in 2022 and 5.9% in 2023, down substantially from its peak of 11.4% in 2020. Alberta's GDP per capita will comfortably exceed the national average of about US$54,900 for 2022. The economy possesses strong fundamentals, despite its concentration in the oil and gas industry. The industry, including supporting activities, typically represents more than 20% of GDP at basic prices, which tempers our economic assessment because of the associated economic and fiscal volatility.

The United Conservative Party (UCP) government, which holds a large majority in the Legislature, has the political capacity to enact reforms despite recent divisions within the party. Premier Kenney resigned as the leader of the UCP on May 18, 2022. The upcoming leadership election could create distraction from the government's agenda, as it also begins to prepare for a general election in May 2023. However, we believe that the province's financial management will continue to maintain prudent fiscal policies. In Budget 2022, the province's fiscal plan for the year focused on strengthening the health care system and the provincial workforce. Alberta's budgets are comprehensive and more detailed than those of other provinces. The province's annual reports comply with Canadian government standards. We consider that the administration is experienced and qualified to prudently manage debt and liquidity, and implement fiscal policies.

As is the case with all provinces in Canada, the ratings also benefit from the very predictable and well-balanced institutional framework in which Alberta operates. The Canadian constitution is the cornerstone of federal-provincial intergovernmental arrangements, which we view as mature and stable. The federal government provides revenue support through a number of agreements and transfer arrangements including the ongoing Canada Health Transfer and Canada Social Transfer payments as well as ad hoc situation-specific transfers such as the pandemic. For fiscal 2022-2023, these transfers will constitute about 19% of operating revenues. Because of higher transfers for child care and fiscal stabilization, total transfers will increase in fiscal 2022-2023, more than offsetting the reduction in pandemic-related transfers. The agreements covering ongoing transfers are long-term, formula-driven, and predictable, but can be subject to change. Typically, the federal and provincial governments discuss proposed changes to transfer programs well ahead of their implementation.

Key Statistics

Table 1

Province of Alberta--Selected Indicators

	--Budget year*--					
(Mil. C$)	**2019**	**2020**	**2021bc**	**2022bc**	**2023bc**	**2024bc**
Operating revenues	45,017	42,589	60,288	64,052	61,900	58,536
Operating expenditures	53,736	55,720	60,024	57,109	56,865	57,648
Operating balance	(8,719)	(13,131)	264	6,943	5,035	888
Operating balance (% of operating revenues)	(19.4)	(30.8)	0.4	10.8	8.1	1.5
Capital revenues	841	548	1,404	1,455	1,074	1,016
Capital expenditures	5,545	6,896	6,619	6,781	5,968	5,414
Balance after capital accounts	(13,423)	(19,479)	(4,951)	1,617	141	(3,510)
Balance after capital accounts (% of total revenues)	(29.3)	(45.2)	(8.0)	2.5	0.2	(5.9)
Debt repaid	33,513	27,329	17,066	17,411	19,721	18,115
Gross borrowings	42,382	48,204	20,743	12,697	20,104	22,069
Balance after borrowings	(4,554)	1,396	(1,274)	(3,097)	524	444
Direct debt (outstanding at year-end)	89,170	108,338	111,651	105,951	109,998	115,581
Direct debt (% of operating revenues)	198.1	254.4	185.2	165.4	177.7	197.5
Tax-supported debt (outstanding at year-end)	92,290	111,512	114,785	109,077	113,071	118,557

Table 1

Province of Alberta--Selected Indicators (cont.)

	--Budget year*--					
(Mil. C$)	2019	2020	2021bc	2022bc	2023bc	2024bc
Tax-supported debt (% of consolidated operating revenues)	205.0	261.8	190.4	170.3	182.7	202.5
Interest (% of operating revenues)	5.0	5.8	4.0	4.2	4.4	4.8
Local GDP per capita (single units)	80,546	66,700	78,965	86,597	90,774	93,365
National GDP per capita (single units)	61,469	58,016	65,266	70,104	71,910	72,783

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. N/A--Not applicable. N.A.--Not available. N.M.--Not meaningful. Budget year 2022 equals fiscal year 2023.

Ratings Score Snapshot

Table 2

Province of Alberta--Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	2
Financial management	2
Budgetary performance	5
Liquidity	2
Debt burden	4
Stand-alone credit profile	a+
Issuer credit rating	A+

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

- Sovereign Risk Indicators, April 11, 2022. Interactive version available at http://www/spratings.com/sri

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- S&P Global Ratings Raises Oil And Gas Price Assumptions On Persistent Geopolitical And Supply Concerns, April 28, 2022
- Economic Outlook Canada Q2 2022: Growth Forecasts Hold up As Global Risks Rise, March 28, 2022
- Institutional Framework Assessment: Canadian Provinces, March 14, 2022
- Sector And Industry Variables Criteria Governments Sovereigns: Sovereign Rating Methodology, Feb. 23, 2022
- S&P Global Ratings Definitions, Nov. 10, 2021
- Guidance: Methodology for Rating Local and Regional Governments Outside of the U.S., July 15, 2019

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Upgraded

	To	From
Alberta (Province of)		
Senior Unsecured	A+	A

Upgraded; Ratings Affirmed

	To	From
Alberta (Province of)		
Issuer Credit Rating	A+/Stable/A-1	A/Stable/A-1

Ratings Affirmed

Alberta (Province of)		
Commercial Paper	A-1	

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.