LAURENTIAN BANK SECURITIES

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Manitoba Public Accounts and First Update Report – Climate Change Brings Volatility

The fiscal update season continues with a better-than-expected FY 2022-23 performance from the Manitoba Province. In a nutshell, climate change standout as the main factor leading to a major swing in economic and fiscal results between this year and the previous one.

The Province of Manitoba ended FY 2021-22 with a net loss of $704M according to the Public Accounts. This $704M deficit nonetheless represents a major improvement relative to the $2.1B shortfall registered during the pandemic time of FY 2020-21. The improvement would have been unambiguously better without adverse climate shocks. First, droughts led to a poor 2021 crop season. Wheat and canola production fell by almost 30% last year. However, elevated commodity prices led to record high farm cash receipts. Second, the drought contributed to a large net loss at Manitoba Hydro struggling with electricity output and export.

As reported through out the 2022 summer season in media and several reports, friendly weather conditions are extremely supportive for an above-average crop year. In a mid-September report, Statistics Canada says Manitoba wheat and soyabeans production are anticipated to jump by 38% and 24% in 2022, respectively. Wheat and soyabean prices stand about 1.7X higher today versus 2021 according to the latest World Bank monthly commodity report. Furthermore, Manitoba Hydro, benefiting from record-high water flows and higher electricity export prices, expects to generate a net positive income in FY 2022-23. This major turnaround from Manitoba Hydro is the main driver behind the major $346M improvement in the Province's deficit in FY 2022-23. The deficit forecast stands at $202M representing a meagre 0.2% of NGDP, down from $548M in the 2022 budget.

Besides the climate-driven influence on Manitoba Hydro's results, there are no meaningful changes to the FY 2022-23 picture. The upside revision in expenses ($191M) is small relative to revenues ($537M). The two upward revisions on the expenses side relate to the tax-free benefit to families in response to high CPI inflation and higher health care spending. Also, the government made the appropriate, conservative choice of keeping taxation revenue unchanged from the budget, recognizing the high degree of uncertainty surrounding the economic outlook. In our view, the tide has shifted due to the very aggressive tightening path proposed by the FOMC. Also, the UK fiscal mismanagement situation created a nonnegligible upward impact on North American interest rates biting even more. Altogether, at least a mild contraction of the U.S. and Canadian economies appears in the cards for early 2023. Accordingly, the 1.9% Manitoba real GDP growth forecast in 2023 included in the First Quarter Report appears unachievable. If a recession indeed becomes reality before the end of FY 2022-23, Manitoba's debt burden will remain very manageable even if the current debt-to-GDP ratio estimate of 33.8% is poised to be revised up. The net debt-to-GDP ratio fortunately plunged from 38% in FY 2020-21 to 35.7% in FY 2021-22.

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