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## Saskatchewan Budget 2021– extended COVID-19 support delays the path to balance

The third pandemic wave is unfolding across the country, including in Saskatchewan. The number of new cases in the Province has been rising since the middle of March. The number of people in intensive care units unfortunately stands at a record high, close to 50. Also, about half of active cases are in the Regina area. Budget 2021 was released on Tuesday in this challenging context.

That being said, the economic plan also relies on the realistic assumption that the vaccine rollout will contribute to improve health outcomes in addition to restore business and consumer confidence. As the IMF highlighted in its latest outlook also released Tuesday, the global economic recovery looks firmer than before due to fiscal stimulus in large countries and the encouraging roadmap toward a vaccine-powered normalization.

### Sustained COVID-19 support and pension revaluation inflate expenses

Without surprise, the much needed but costly government response to the pandemic is at the heart of the budget plan. COVID-19 support, including $123M for health and public safety and $1.4B in economic support will cost $1.5B in FY 2021-22, part of a $4.8B multi-year pandemic response plan. Besides health care, the largest single item contributing to rising expenses is a $415M accrual adjustment to pension plan expenses, mainly reflecting a decrease in the discount rate used to value pension liabilities. Most ministries will see additional funding to support export development and growth in the technology sector. Overall, program expenses will increase by 7.1% from last year to reach $16.3B in FY 2021-22.

### Upside risks to the revenue outlook

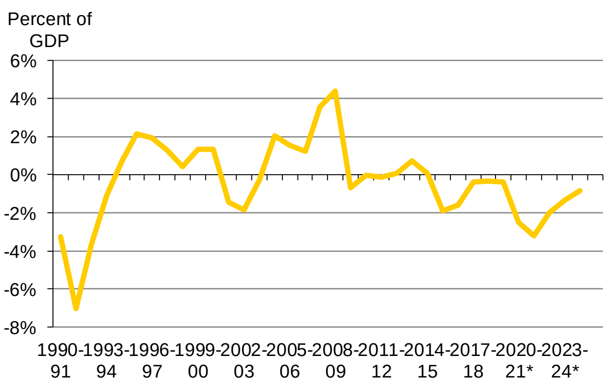
On the revenue side, Saskatchewan projects a 2.7% rebound, to $14.5B. This follows a 5.3% contraction in FY 2020-21, the largest decline in over 10 years. Taxation revenue increases 7.9% in FY 2021-22, without introducing major tax changes. In relation to the 3.4% Saskatchewan real GDP growth forecast for 2021, and considering the significant positive revisions to our economic outlook in April, we see upside risks to the province's taxation revenue forecast this year. Similar to what we've seen so far in this budget season, the Saskatchewan government anticipates a $300M drop in federal transfers, to $2.9B, in FY 2021-22. This does not include the recently announced $124M one-time federal health transfer as part of Bill C-25.

In our view, the global environment will become particularly more favourable for the Province's non-renewable resource revenue, projected at $1.3B in FY 2021-22, up $0.2B from the previous year. With respect to the global potash market, recent contracts signed between India and European producers revealed a significant jump in pricing relative to contracts signed earlier this year. As for the global oil market, OPEC+ announced at the beginning of April that it would gradually taper its voluntary output cuts starting in May. The pace of reduction in output cuts should be slow enough to prevent renewed imbalances between supply and demand, therefore supporting current WTI oil prices at around US$60/bbl over the next quarters. Stronger-than-expected oil prices, as well as narrower-than-projected WTI-WCS spread represent additional upside risks to the revenue outlook.

**Shrinking deficits over the horizon but incomplete plan toward a balanced budget**
All in all, a large $2.6B deficit is penciled in for FY 2021-22 (3.2% of GDP), wider than the $1.9B shortfall forecast for FY 2020-21, broadly unchanged from the November mid-year update (chart 1).

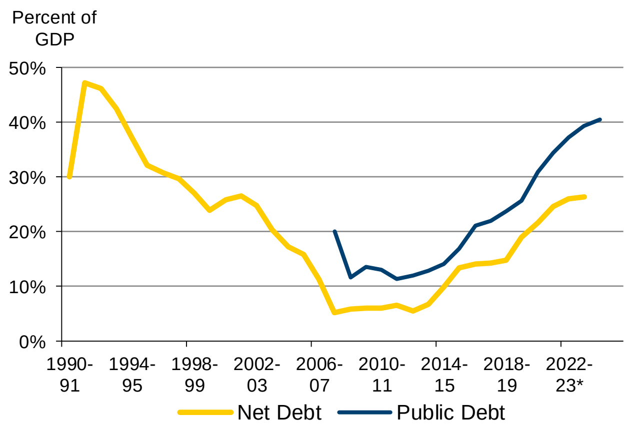
Premier Scott Moe and Finance Minister Donna Harpaeur did hint about the difficulty of eliminating the deficit by FY 2024-25 in recent weeks, an objective set during the Fall 2020 election campaign. The budget confirms the abandon of this goal, referring instead to a return to balance in FY 2026-27. The budget does not include forecasts post-2025, and thus does not provide a complete path toward balance. The four-year financial framework shows shrinking deficits of $1.7B in FY 2022-23 (2% of GDP), $1.2B in FY 2023-24 (1.3% of GDP) and $0.8B in FY 2024-25 (0.9% of GDP) supported by a gradually improving revenue outlook and virtually flat average annual growth in total expenses.

Chart 1: Saskatchewan Budgetary Balance




Sources: Sask. Gvt, Government of Canada Fiscal Reference Tables, LBS Econ. Res. and Strategy.

Chart 2: Saskatchewan Debt Measures




Source: Sask. Gvt, Government of Canada Fiscal Reference Tables, LBS Econ. Res. and Strategy.

**Debt levels go up but will remain comparatively low and manageable**
These deficits, on top of the record capital plan to support the recovery, will lead to a steady rise in public debt, from about $21.3B when the pandemic began in March 2020, to $36.4B five years later in March 2025 (40.5% of GDP, chart 2). Net debt-to-GDP is expected to follow a similar path, from 14.8% in FY 2020-21, it is projected to reach 26.3% in FY 2024-25. A deteriorating debt profile was the key driver behind Moody's negative outlook on the province's Aaa rating in September 2020: "a faster-than anticipated rise in the debt burden that will weaken the province's credit profile to a level no longer consistent with Aaa-rated peers". Nonetheless, Saskatchewan credit ratings remain strong: AA by S&P and AA(low) by DBRS.

Finally, the 10-year Canadian bond yield projection used in this budget shows a very mild increase to less than 1.5% by 2024. This assumption was likely made before the recent increase in global interest rates, which opens the door to higher-than-expected public debt charges. Still, the province exhibits the lowest debt burden among provincial jurisdictions, meaning the possibility of higher debt servicing costs will not materially change the overall financial picture. About 4.4 cents on every dollar spent go to service the debt in Saskatchewan, relative to 4.9 cents in Alberta, 6.9 cents in Ontario and 6.8 cents in Quebec. Borrowing requirements are projected at $4.1B, excluding short-term debt, close to last year's longer-term financing needs of $4.5B.

In summary, the Saskatchewan government privileged, like all other provinces that have released their budgets in recent weeks, the necessity to spend their way out of the pandemic. The relatively low public debt burden of Saskatchewan provides the government the opportunity to put aside , fiscal consolidation, at least until the definitive end of the pandemic.

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