

CREDIT OPINION

31 January 2023

Update

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RATINGS

Alberta, Province of

Domicile	Canada
Long Term Rating	Aa2
Type	Senior Unsecured - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Province of Alberta (Canada)

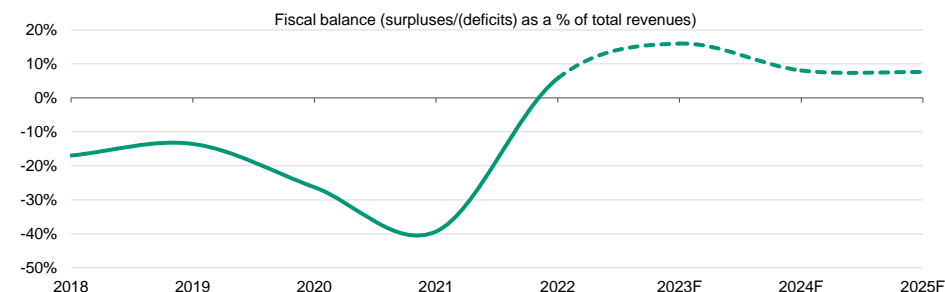
Update following rating upgrade

Summary

The credit profile of the [Province of Alberta](#) (Aa2 stable) reflects our forecast of continued fiscal surpluses supported by sustained high oil prices above pre-pandemic levels. The strong revenue growth and low new debt accumulation significantly reduced the debt burden from its 2021 peak, with our estimate of net direct and indirect debt at 143.4% of revenue in 2022-23 and largely similar levels until 2024-25. Alberta also maintains a very strong liquidity profile, and a competitive tax regime relative to peers. The province faces pressures from its exposure to the volatility in oil prices which creates significant swings in fiscal results, and from carbon transition risk. Inflationary pressures could also lower fiscal outcomes, although in our view the province will generate sufficient revenues to offset inflationary expense pressures and maintain positive results.

Exhibit 1

Economic rebound and high oil prices contribute to a significant fiscal improvement



Fiscal years ending March 31

Sources: Province of Alberta and Moody's Investors Service

Credit strengths

- » Projected fiscal surpluses tied to oil revenue and general economic rebound
- » Excellent levels of liquidity from cash and investments
- » Moderate debt burden due to much improved debt profile
- » Competitive tax regime and fiscal flexibility within a mature institutional framework

Credit challenges

- » Dependence on oil exposes province to price volatility and carbon transition risk
- » High inflation and macroeconomic uncertainties will pressure fiscal results

Rating outlook

The stable outlook reflects Moody's view that the fiscal improvements from continued projected surpluses and significantly lower debt levels over the next two years will allow the province to balance the key pressures from inflation and fluctuating resource prices.

Factors that could lead to an upgrade

The rating could be upgraded if the province's fiscal position continued to improve despite higher inflation and interest rates, allowing the province to reduce its net direct and indirect debt to below 130% of revenue on a sustained basis. A larger increase in liquidity balances than under our current projection would also put upward pressure on the rating.

Factors that could lead to a downgrade

The rating could be downgraded if lower than projected revenues, coupled with a slowing economic recovery, lead to a return to material consolidated deficits and result in a trajectory of materially increasing debt burden.

Key indicators

Exhibit 2

Province of Alberta
Year ending March 31

(Year Ending March 31)	2020	2021	2022	2023F	2024F	2025F
Net Direct and Indirect Debt as a % of Revenues	202.7	254.0	160.4	143.4	149.3	146.1
Net Direct and Indirect Debt as a % of GDP	26.6	36.9	29.3	28.3	25.0	23.5
Cash Financing Surplus (Requirement) as a % of Revenues	(23.0)	(50.1)	(9.9)	9.8	0.7	(7.5)
Consolidated Surplus (Deficit) as a % of Revenues	(26.3)	(39.3)	5.8	16.0	8.1	7.6
Total Interest Expense as a % of Revenues	4.8	5.8	3.9	3.5	4.0	3.7
Intergovernmental Transfers as a % of Revenues	19.6	24.4	17.0	16.2	16.6	17.6
Real GDP Growth (%) [1]	(7.7)	4.8	4.8	2.7	2.9	2.8

[1] Calendar year, 2023-2025 are provincial forecasts

Sources: Province of Alberta and Moody's Investors Service

Detailed credit considerations

On January 25, 2023, we upgraded Alberta's ratings to Aa2 from Aa3 and revised the outlook to stable. The upgrade reflects our view that the fiscal and economic rebound which began in 2021-22 and carried forward into 2022-23 led to an improved risk profile with ongoing surpluses and a significant reduction in the debt burden relative to our previous forecasts.

The credit profile of the Province of Alberta, as expressed in its Aa2 rating, combines a Baseline Credit Assessment (BCA) of aa3, and a high likelihood of extraordinary support from the [Government of Canada](#) (Aaa stable) should the province face acute liquidity stress.

Baseline Credit Assessment

Projected fiscal surpluses tied to oil revenue and general economic rebound

Following record deficits in 2019-20 and 2020-21, Alberta returned to balance in 2021-22, several years ahead of its earlier projection and marking the first time the province posted a surplus since 2014-15. The province now forecasts a record surplus of CAD12.3 billion, or 16.0% of revenue for 2022-23 and continued surpluses for 2023-24 and 2024-25 averaging CAD5.5 billion, or 7.8% of revenue.

Much of the improvement is tied to rising non-renewable resources revenue primarily from oil, which reflects the strong recovery in oil prices as the demand surged amid global uncertainty and pushed prices above \$120/barrel in 2022. Despite prices falling from the mid-2022 highs, oil-related revenues will contribute an estimated CAD23.4 billion (30.4%) of total revenue in 2022-23. Over the following two years, the province projects more normalized levels of resource revenue, forecasted to average 21.2% of total revenues.

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This projections are based on the province's assumptions of the West Texas Intermediate (WTI) oil price averaging \$78.50/barrel in 2023-24 and \$73.50/barrel in 2024-25, moderately above the Moody's medium-term forecast of \$50-70/barrel.

The oil price dynamics also coincide with overall improving economic conditions in the province, with real GDP growth estimated to exceed the Canadian growth rate, which Moody's projects at 3.3% in 2022 and 0.6% in 2023, as business and consumer spending increase leading to rising tax and other revenues.

The province projects nominal total expense growth of 0.4% for 2022-23 and flat growth by 2024-25, below revenue growth, mainly due to a combination of spending restraint in health and education expenses, and lower than previously projected interest expense. At the same time, the reduced need for COVID support and initiatives is partly being replaced by ongoing affordability initiatives totalling CAD 1.3 billion for 2022-23 and CAD 1.5 billion for 2023-24 to 2024-25, including rebate cheques to help individuals combat high inflation.

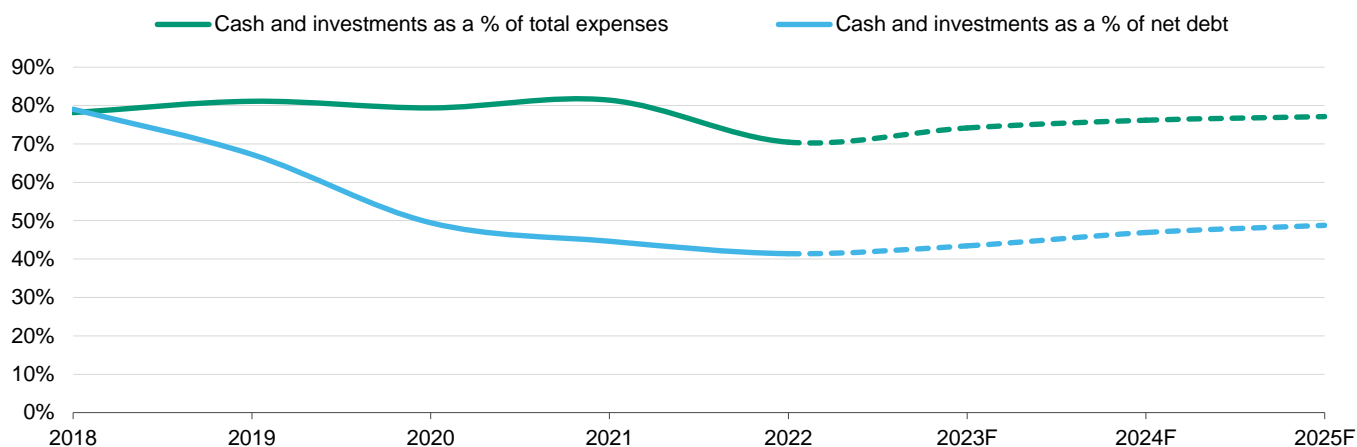
Excellent levels of liquidity from cash and investments

The province's wealth metrics are very strong relative to its domestic peers, with our projection of combined cash and investments totalling CAD47.9 billion at March 31, 2023. We estimate that cash and investment balances will cover approximately 74% of expenses and 43% of net debt in 2022-23.

The high level of cash and investments provides a buffer for bondholders against fiscal shortfalls and rising expenses including debt costs. We project that these balances will continue to grow given the anticipated surpluses, providing continued strong coverage against debt levels and expenses.

Exhibit 3

High levels of cash and investment will continue to provide strong coverage ratios Fiscal years ending March 31



Sources: Province of Alberta and Moody's Investors Service

Nearly 40% of balances is invested in the Alberta Heritage Savings Trust Fund (CAD18.5 billion book value estimated for 2022-23), a long-term savings fund created to invest a portion of Alberta's oil revenue for the benefit of future generations and one of the largest wealth funds globally. Although the province's mid-year 2022-23 fiscal update abandoned its earlier explicit pledge to contribute CAD1.7 billion of surpluses to the Heritage fund in 2022-23, we project continued growth in the fund from anticipated surpluses and from retaining returns within the fund for inflation protection. Although the fund's asset composition is well diversified, a relatively high allocation to equities and alternative investments exposes it to asset value and performance fluctuations.

Moderate debt burden due to much improved debt profile

Alberta's debt burden rose significantly between 2014-15 and 2021-22 to exceed 250% of revenue in 2020-21, with much of the debt issued to finance large deficits that resulted from weaker natural resource revenues and exacerbated by the fiscal pressures caused by the pandemic. However, the improvement in the province's fiscal results with surpluses in 2021-22 and forecasted for 2022-23 to 2024-25 have now significantly reduced the government's borrowing needs. Compared to Budget 2022-23, which already indicated

an improved borrowing requirement compared to the preceding budget, debt needs are now estimated to be CAD11 billion lower between 2022-23 and 2024-25 as the province is looking to prioritize repaying maturing debt obligations from its surpluses and cash position. The province intends to use 75% of its excess cash surpluses over the next few years for the purpose of debt repayment with the remaining allocated to savings and future-year debt repayments.

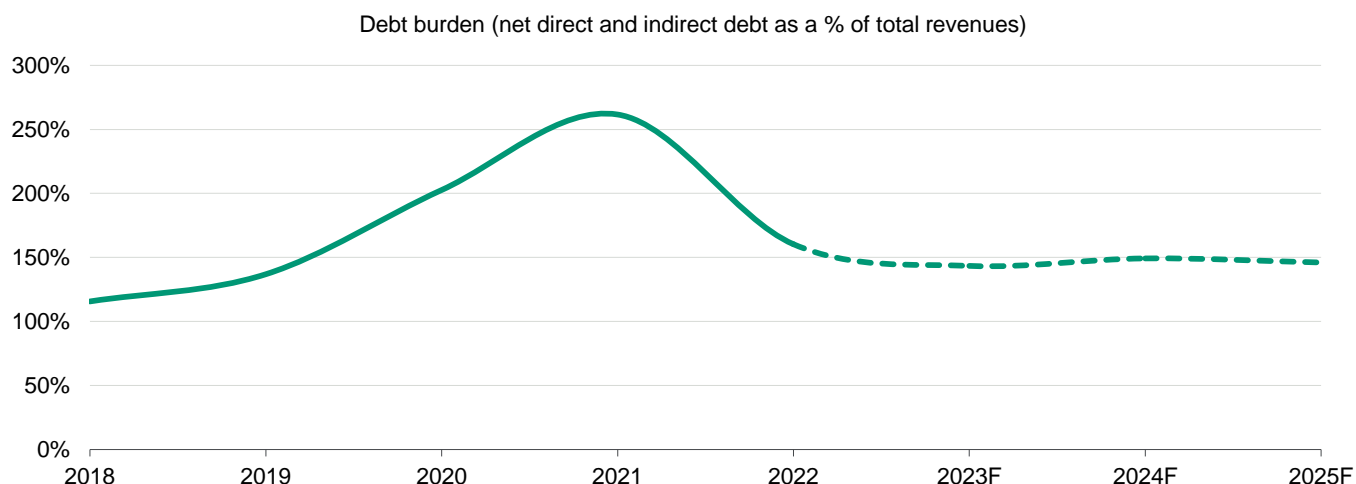
We expect that the debt burden will fall to pre-pandemic levels, with an estimate of net direct and indirect debt at 143.4% of revenue in 2022-23. We also project similar debt levels for 2023-24 and 2024-25 as gradually declining debt levels will coincide with declining revenue as oil prices normalize and pandemic-related federal support declines.

Debt will be issued to support capital spending, with capital spending estimated to total CAD20.2 billion between 2022-23 and 2024-25, including for new large-scale healthcare initiatives. We estimate that up to 60% of the capital plan could be financed through debt.

The improvement in the debt burden is supported by improved debt affordability, with our estimate of interest expense at around 3.5% to 4.0% over the next two years, as the pressures of elevated interest rates will be balanced by the reduced debt issuance needs.

Exhibit 4

Strong revenue growth and positive fiscal results have led to an improvement in the debt burden
Year ending March 31



Sources: Province of Alberta and Moody's Investors Service

Competitive tax regime and fiscal flexibility within a mature institutional framework

Alberta retains access to a broad range of tax bases and the ability to alter expenditure programs. Alberta's tax regime remains highly competitive relative to most provincial peers in respect of both corporate and personal income tax rates, providing the province with greater fiscal capacity and an attractive location for individuals and businesses seeking a tax advantage. For example, marginal personal income rates range between 10% and 15%, one of the lowest levels in Canada. The province's corporate tax rate is the lowest in the country, following an accelerated reduction in the corporate tax rate to 8% from 12% in 2020. Alberta also does not levy a health premium or payroll taxes, and remains the only Canadian province without a provincial sales tax.

The tax regime provides the province with significant capacity to enact future tax measures to support revenue growth if necessary and still remain competitive with other provinces. Nevertheless, policy actions in recent years have focused on increasing or maintaining tax competitiveness. As a result, we do not expect a material reversal of these policies in the near future that would lead to higher tax revenues.

Alberta has significant flexibility in its financial management in both revenue and expenditure measures to achieve budget targets and move forward with its plan to balanced budgets. Similar to other Canadian provinces, Alberta has greater fiscal autonomy compared with its counterparts in other countries, such as the German Länder and the Australian states. As such, the province has a high degree

of fiscal policy flexibility that is more akin to that of sovereign governments than many of their international sub-sovereign peers. This framework provides the province with unfettered access to a broad range of tax bases and wide discretion over expenditure decisions, endowing it with substantial flexibility to address fiscal challenges.

The institutional framework governing relations, powers and responsibilities between Alberta and the federal government is well developed and stable. A system of fiscal transfers from the federal government, including health and social transfers that increase based on pre-determined escalators, also supports Alberta's credit profile. These transfers are highly predictable and secure and mitigate macroeconomic volatility. Historically, these federal transfers accounted for a 15-20% share of Alberta's total revenues.

In addition to the major federal transfers to the province, over the last three years Alberta has also benefited from additional federal support including a one-time health transfer, a top-up for gas tax rebates and fiscal stabilization transfers to offset revenue shocks, although we do not expect that these transfers will accrue in future years.

Dependence on oil exposes province to price volatility and carbon transition risk

Changes in oil prices exhibit significant volatility as prices and volumes react to OPEC decisions and changes in global geopolitical risks, and this was evident in the range in oil prices of \$50/bbl in 2022. The continued reliance on oil as a key revenue driver and the most significant non-renewable resource of the province (80%-85% of natural resource revenue derives from bitumen and crude oil royalties) exposes the province to significant swings in its fiscal results and considerable forecast uncertainty. In our view, this is one of the key credit challenges facing the province.

Alberta's resource revenues are also exposed to changes in the light-heavy oil price differential, which are impacted by pipeline egress issues and transportation costs. A wider differential has a negative impact on the province's bottom line as it reduces royalty revenue relative to WTI prices. The province's November 2022 fiscal update expects higher differentials for 2022-23 to 2024-25 than budget, averaging U\$19.80/barrel for 2022-23 and falling to \$16.10/barrel by 2024-25. The fiscal sensitivity to oil price changes is significant and can therefore result in significant revenue fluctuation, estimated at CAD500 million for each \$1/bbl change in WTI prices, and CAD460 million for each \$1 change in the light-heavy differential.

As Canada's largest oil producer, and with a high share of revenue oil production, Alberta is more susceptible to carbon transition risk than any other province and many global regional peers, especially as decarbonization efforts and the transition towards cleaner energy continues. Although Alberta imposes a price on carbon which must meet federal requirements, changes in federal policy decisions could create discrepancies between provincial and federal policies with additional costs for the province.

High inflation and macroeconomic uncertainties will pressure fiscal results

Although Alberta benefits from the rise in global demand for Canadian energy, slowing global economic growth, high inflation and supply chain constraints create risks that could negatively impact fiscal results. While we do not anticipate that these factors would lead to material changes in Alberta's credit metrics, a slower global economic growth would impact business and consumer confidence resulting in weaker revenue growth, especially tax and business enterprise revenue, while spending pressures from inflation will continue to be elevated. The province's November 2022 fiscal update already projects an increase of CAD1.3 billion in total expenses relative to its Budget 2022-23 due to higher provision for inflation, including a fuel tax relief program and the indexation of personal income taxes to inflation.

The global growth outlook for 2023 has weakened considerably over the last year, with global trade slowing and inflation being more persistent than previously projected, although inflation has started to cool in recent months. Accelerated policy tightening by the Bank of Canada, after more than a decade of historically low rates, to combat rising domestic inflation led to increasing interest rates which will increase Alberta's cost of funding. However, with the vast majority of debt issued under fixed interest rates and low debt requirements forecasted, the province is minimally exposed to the impact of elevated rates with regards to debt service across the next 3-4 years.

The province will face pressure from its workforce to adjust salaries and wages to offset the impact to real income from the high inflationary environment especially in a period of very tight labour conditions in Canada. While the province will benefit from multi-year collective agreements with the majority of its labour force, with staggered expiration dates that will delay the impact of higher wages, as these contracts expire we anticipate unions will seek pay increases much higher than recent past contracts. At the same time, elevated inflation will increase the cost of construction labour and materials, putting long-term upward pressure on capital spending.

Extraordinary support considerations

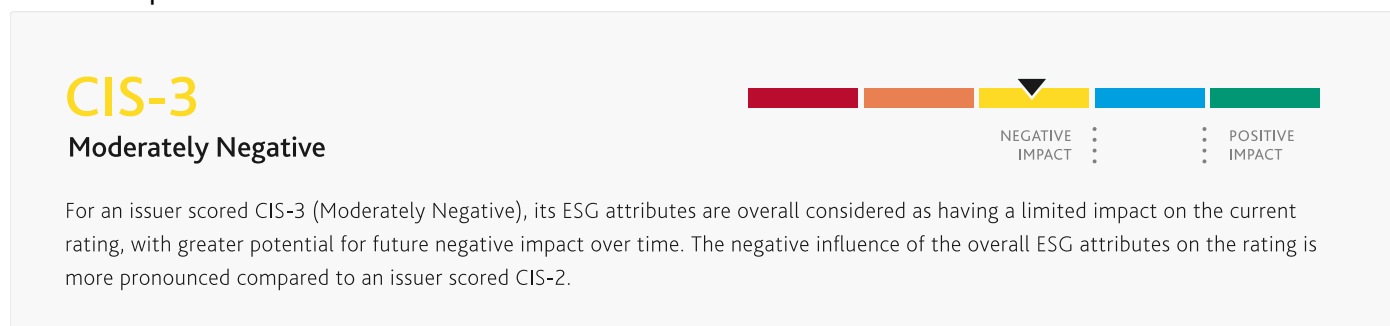
We assign a high likelihood that the Government of Canada would act to prevent a default by Alberta. The high likelihood of support reflects our assessment of the federal government's incentive to minimize the risk of potential disruptions to capital markets if Alberta or any province were to default. It also indicates a moderately positive federal government policy stance, as illustrated by the flexibility inherent in the system of federal-provincial transfers.

ESG considerations

Alberta's ESG Credit Impact Score is Moderately Negative CIS-3

Exhibit 5

ESG Credit Impact Score

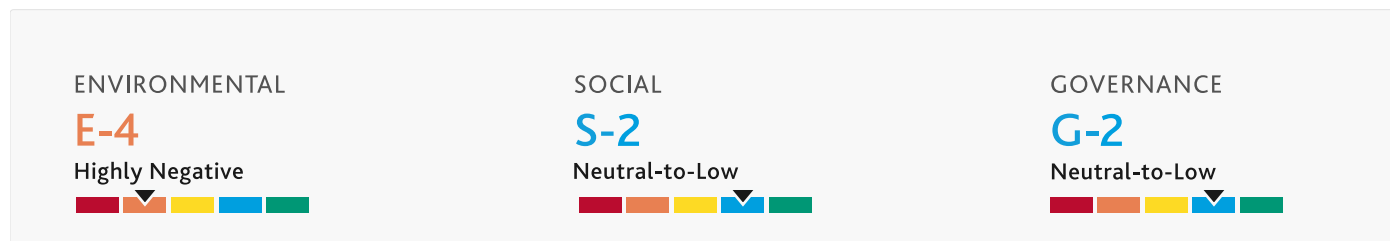


Source: Moody's Investors Service

Alberta's ESG Credit Impact Score is moderately negative (**CIS-3**) reflecting highly negative exposure to environmental risks, neutral-to-low exposure to social risks and neutral-to-low governance risk.

Exhibit 6

ESG Issuer Profile Scores



Source: Moody's Investors Service

Environmental

The E issuer profile score is highly negative (E-4) which reflects exposure to carbon transition risk and elevated exposure to physical climate risks. Alberta is the nation's biggest oil producer which contributes to a significant portion of GDP and revenues, and therefore Alberta is more susceptible to carbon transition risk than most other provinces and global regional peers as decarbonization efforts and the transition towards cleaner energy continues. Although Alberta imposes a price on carbon which must meet federal requirements, changes in federal policy decisions could create discrepancies between provincial and federal policies. At the same time, exposure to physical climate risks is elevated given unpredictable weather events including periodic droughts and wildfires which can cause significant economic damage.

Social

Alberta's S issuer profile score is neutral-to-low (S-2). Health and safety measures and access to infrastructure in the province is strong, and housing affordability is high relative to several other provinces. Alberta has the youngest overall provincial population, which mitigates healthcare spending pressures while increasing education spending relative to other Canadian provinces. These strengths are partly offset by reduced job opportunities in the oil sector and elevated unemployment rates.

Governance

Alberta's G issuer profile score is neutral-to-low (G-2). The institutional and governance framework inherent to all Canadian provinces is strong, with transparent reporting and disclosure. The province's efforts to prioritize debt reduction supports strong debt management. Public accounts and budgets are typically prepared on a timely basis.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Rating methodology and scorecard factors

The assigned BCA of aa3 is in line with the scorecard-indicated BCA of aa3. The scorecard-indicated outcome of aa3 reflects (1) an idiosyncratic risk of 4 (presented below) on a 1 to 9 scale, where 1 represents the strongest relative credit quality and 9 the weakest; and (2) a systemic risk of Aaa, as reflected in the sovereign bond rating of the Government of Canada (Aaa stable).

For details of our rating approach, please refer to [Rating Methodology: Regional and Local Governments](#), January 16, 2018.

Exhibit 7

Province of Alberta Regional & Local Governments

Baseline Credit Assessment – Scorecard	Score	Value	Sub-factor Weighting	Sub-factor Total	Factor Weighting	Total
Factor 1: Economic Fundamentals				2.20	20%	0.44
Economic Strength [1]	1	125.10%	70%			
Economic Volatility	5		30%			
Factor 2: Institutional Framework				1	20%	0.20
Legislative Background	1		50%			
Financial Flexibility	1		50%			
Factor 3: Financial Position				4.25	30%	1.28
Operating Margin [2]	7	-4.57%	12.5%			
Interest Burden [3]	5	4.55%	12.5%			
Liquidity	1		25%			
Debt Burden [4]	7	160.35%	25%			
Debt Structure [5]	3	19.65%	25%			
Factor 4: Governance and Management				5	30%	1.50
Risk Controls and Financial Management	5					
Investment and Debt Management	1					
Transparency and Disclosure	1					
Idiosyncratic Risk Assessment						3.42 (3)
Systemic Risk Assessment						Aaa
Scorecard-Indicated BCA Outcome						aa3
Assigned BCA						aa3

[1] Local GDP per capita as % of national GDP per capita

[2] Gross operating balance by function/operating revenues

[3] (Adjusted) interest expenses/operating revenues

[4] Net direct and indirect debt/operating revenues

[5] Short-term direct debt/total direct debt

Source: Moody's Investors Service; Fiscal 2021.

Ratings

Exhibit 8

Category	Moody's Rating
ALBERTA, PROVINCE OF	
Outlook	Stable
Baseline Credit Assessment	aa3
Senior Unsecured	Aa2
Commercial Paper	P-1
ATB FINANCIAL	
Outlook	Stable
Issuer Rating -Dom Curr	Aa2
ST Issuer Rating -Dom Curr	P-1
ALBERTA CAPITAL FINANCE AUTHORITY	
Senior Unsecured -Dom Curr	Aa2

Source: Moody's Investors Service

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