Market View
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And now, please welcome to the stage… the B-52s

By Warren Lovely

No, not the **B**and but the **B**ond… a new Ontario **2052** Canadian dollar benchmark long bond to be precise. Canada's provinces aren't letting summer vacation interfere with their borrowing plans. Even though requirements appear biased lower and borrowing programs are appropriately advanced, expect provinces to seize on available issuing windows. That's likely to include the establishment of a new 30-year CAD benchmark from Ontario. Some context ahead of the prospective new issue, supplemented by detailed tables on page 2:

- Ontario's next 30-year benchmark should bear a December 2, 2052 maturity date. When it arrives, the new bond will close the book on the ONT 1.9% Dec-2051s, originally launched last August and tapped 17X, leaving current outstandings at C$12.75 billion. If you're counting, the 2051s bring to eight the number of consecutive Ontario 30Y benchmarks with a float exceeding C$10 billion—testifying to the excellent liquidity afforded investors by Canada's large provinces. Trivia: The last Ontario 30Y benchmark bond where outstandings fell shy of 10 yards was the ONT 4.6% Jun-2039s, a bond launched before the full impact of the GFC took hold and which now feels like a lifetime ago;
- Ontario likely won't waste much timing building its new bond up to size. The first 30Y re-opening typically occurs within two weeks (if not mere days). The C$2 billion o/s threshold has been hit inside of a month the last couple go-rounds, the C$5 billion level breached within 180 days (on average). Notwithstanding demonstrated access to international markets and evident demand in other domestic tenors, Ontario's elevated borrowing program (currently C$53.9 billion) implies ample scope to build the upcoming 30Y relatively quickly;
- Based on prevailing levels, the new bond might bear a coupon in the vicinity of 2½%. While no match for the record low coupon attached to the 2051s, that could well be the second lowest 30Y coupon on record. Moreover, nominal borrowing rates even at the furthest reaches of the curve remain shy of the province's inflation rate (averaging 3.1% over the past three months) and are thus negative in real terms;
- Notwithstanding COVID-related scars, Ontario's new 30Y bond is still likely to sport a tighter-than-average NI spread. As always, the precise timing and spread will hinge on market tone and investor sentiment. At the moment, Ontario's 2051 bond trades ~80 bps over CAN 2051s. Assuming the new issue is priced flat to 0.5 bps back of the existing benchmark, the new issue spread could be some 10 bps tighter than the average launch level in the post-GFC world. In the past decade, only the 2049s issued at a tighter absolute spread than today;
- Regardless of the exact launch date, it looks as though the WI 2052s will buck the prior tendency towards inversion in the pricing of new Ontario 30-year benchmarks. Last summer, the 2051s launched a snick (-0.5 bp) inside of the old bond. Prior to that, both the 2050 and 2049 bonds were priced -1 bp to existing benchmarks. Even further back, the green banner for the 2048s went up at equivalent of -0.5 bps vs. the prior benchmark. By our count, the last time a new 30Y came flat to the 'olds' was the 2046 issue (launched in 2015). Note that long end inversions have gone away in provi land more generally, a by-product of more serious and steady GoC supply (including extra-longs). Investors could notionally move from Ontario 2051s to a new bond and shorten duration by roughly 1 unit without giving on spread;
- More than nixing the NI inversion, Ontario longs continue to offer meaningful/above-average yield enhancement over the current 10-year benchmark (about 40% excess yield at the time of writing). Considering the recent rally in underlying rates markets, it's clear that Ontario longs provide some welcome juice vs. skinnier yields/spreads down the curve. We'd note that the 10s-30s credit box, which at ~20 bps on a constant maturity basis, is *far* steeper than prior go rounds—essentially double the average where prior 30Y bonds were birthed;
- RV wise, the new Ontario bond should come at the 'cheaper' end of the range vs. where other provinces trade in the long end. As it stands, the average 30Y basis to Ontario has snugged up to ~7 bps or less than 10% of the underlying Ontario spread. In prior iterations, the non-Ontario basis was more like 10-25 bps. So investors will need to give up a lot less spread (on a relative basis) to go into the new Ontario;
- Ontario's new 30-year issues have cultivated a respectable (if unspectacular) performance record vs. Canadas. We typically don't see a meaningful move tighter (vs. the pricing bond or the 'olds') right away. After 10, 20 or 50 sessions, however, the new bond has (on average) tightened by 1-3 basis points vs. Canadas, retaining if not gaining a tiny bit of ground vs. older Ontario bonds as a benchmark premium gradually develops. Based on prevailing levels vs. the GoC curve and interpolated 'fair value' from 10Y to 30Y, we'd currently peg Ontario's 30-year liquidity premium at 1.3-1.8 bps for each year you move away from the on-the-run security;
- Five provinces have launched new 30Y benchmarks since the Ontario 2051s arrived. British Columbia and Quebec were the two most recent cases, producing little in the way investor indigestion as judged by absolute/relative spread metrics. If anything, the long basis for both Alberta and Saskatchewan tightened nicely in the wake of their new bonds, part of a broader compression in credit at that time;
- We caution against placing blind faith in the empirical performance record. Not all else is equal. The virus situation is clearly unsettled, policy in some cases in flux. Related developments can/will impact global risk sentiment, as witnessed in recent sessions. There's a lot more 30Y supply coming from Canada's sovereign relative to pre-COVID times, and BoC tapering means QE is absorbing fewer Canada bonds at a margin. As a reminder, part of the BoC's CE effort (in the form of provi bond purchase facility) faded to black back in the spring;
- Market seasonals should likewise be interpreted with caution, which are something of a mixed bag in Q3—generally solid July spread performance typically giving way to some leakage in spreads in August-September. It's likely a bit premature, but keep the eventual September 1st cash flow effects in mind, related Index adjustments tending to spark marginal demand for duration all else being equal;
- Fundamentally, Ontario is in recovery mode. Notwithstanding Delta variant worries, economic growth should seriously top budget expectations in 2021. We anticipate 10% nominal growth, whereas the March budget is based on a much more conservative 6.2% figure, a gap worth billions to own-source revenues. So while Ontario has planned for a budget deficit of C$33.1 billion in 2021-22, we see ample scope to better the budgetary target. Notably, Ontario's four long-term credit ratings (from S&P, Moody's, Fitch, DBRS) have all been affirmed in recent weeks, in all cases maintaining a "stable" outlook. So while intrinsic credit quality in the broader provincial sector remains under some pressure, Ontario's ratings do not appear at risk in the near term.

Table 1: A closer look at the development of Ontario's 30-year domestic benchmarks

Introduction, development & performance of Ontario C$ 30-year benchmark bonds

Maturity	Coupon	First issued	Latest/last re-opening	Total issued	Times issued	First issue size	Average R-O size	Time to first R-O	Days to reach O/S amount: $2bln	$5bln	$7bln	Spread level & change vs GoC compared to close of NI day: NI close	Bench	+1D	+5D	+10D	+20D	+50D
date	*%*	*date*	*date*	*$mln*	*#*	*$mln*	*$mln*	*days*	*days*	*days*	*days*	*bps*	*CAN*	*bps*	*bps*	*bps*	*bps*	*bps*
12/02/2051	1.9	08/18/2020	07/06/2021	12,750	18	600	715	8	28	171	225	85	*12/51*	1	1	-3	-3	2
12/02/2050	2.65	05/24/2019	07/16/2020	14,100	19	600	750	11	20	138	172	82	*12/51*	0	2	1	-3	-4
06/02/2049	2.9	11/28/2017	05/14/2019	13,250	18	750	735	20	134	178	267	70	*12/48*	0	0	-1	-4	0
06/02/2048	2.8	06/16/2016	09/25/2017	12,700	18	600	712	13	40	176	336	107	*12/48*	-1	-6	-5	-9	-9
12/02/2046	2.9	01/28/2015	05/31/2016	14,700	20	750	734	1	22	141	180	92	*12/45*	0	-6	-5	-7	-8
06/02/2045	3.45	05/07/2013	12/03/2014	16,050	24	750	665	22	63	202	268	100	*12/45*	0	0	-2	-1	-2
06/02/2043	3.5	01/26/2012	04/04/2013	11,200	17	600	663	13	41	195	295	86	*12/45*	0	2	0	2	12
06/02/2041	4.65	06/10/2010	12/02/2011	11,650	18	600	650	34	109	239	335	92	*6/41*	0	3	0	1	-1
06/02/2039	4.6	01/10/2008	08/31/2010	9,700	22	600	433	109	168	692	840	56	*6/37*	0	-1	2	2	12
06/02/2037	4.7	02/17/2006	12/04/2007	9,100	17	500	538	77	154	353	558	58	*6/37*	0	2	4	0	-5
Average	3.09	*Post GFC, NEW 30Y typically*		13,300	19	656	703	15	57	180	260	89.3		-0.1	-0.5	-2.0	-2.9	-1.1
Median	2.90	*established every 15-20 months,*		13,000	18	600	713	13	41	177	268	89.1		0.0	0.7	-1.7	-3.0	-1.6
Min	1.9	*but timing/maturity somewhat*		11,200	17	600	650	1	20	138	172	70		-1	-6	-5	-9	-9
Max	4.65	*less rigid than 10Y*		16,050	24	750	750	34	134	239	336	107		1	3	1	2	12

Notes: These tables show the evolution of NEW Ontario 30-year benchmark bonds; the dotted line separates post-GFC crisis from prior period (on basis of new issue date); average, median, min and max values relate to bonds first issued in post-GFC period (i.e., 2041-2051 maturities); all dollar amounts are par value; "R-O" refers to re-opening; "O/S" refers to outstanding; "NI" refers to new issue; in some cases, benchmark GoC bond used for spread calculations may not have been original pricing bond

Source: NBF, Bloomberg

Table 2: Underlying market context prior to launch of Ontario's earlier 30-year bonds vs. now

Underlying GoC/Ontario yields and curves prior to Ontario launching new C$ 30-year benchmark bond, including other economic/financial market indicators for reference

New 30Y BM	Day before NI	GoC benchmark bond yield 10Y	30Y	10Y-30Y		Ontario yield (existing benchmark) 10Y	30Y	10Y-30Y		Ontario spread vs. GoC 10Y	30Y	10Y-30Y		US IG CDX 5Y	Equity vol (VIX)	Cdn dollar	Jobless rate	Credit ratings S&P	Moody's
maturity	*date*	*%*	*%*	*bps*	*ratio*	*%*	*%*	*bps*	*ratio*	*bps*	*bps*	*bps*	*ratio*	*bps*	*index*	*vs. USD*	*%*	*LT|outlook*	*LT|outlook*
2052 WI	*Current**	*1.22*	*1.80*	*57.3*	*1.47*	*1.87*	*2.60*	*73.2*	*1.39*	*60*	*80*	*20*	*1.33*	*49*	*18*	*1.25*	*8.4*	*A+|Stb*	*Aa3|Stb*
2051	08/17/2020	0.58	1.10	51.2	1.88	1.31	1.95	63.8	1.49	73	85	13	1.17	67	21	1.32	10.6	A+|Stb	Aa3|Stb
2050	05/23/2019	1.64	1.88	24.4	1.15	2.37	2.71	33.4	1.14	73	82	9	1.12	65	17	1.35	5.3	A+|Stb	Aa3|Stb
2049	11/27/2017	1.86	2.22	35.8	1.19	2.48	2.93	45.4	1.18	61	71	10	1.16	54	10	1.28	5.7	A+|Stb	Aa2|Stb
2048	06/15/2016	1.08	1.76	67.7	1.63	2.05	2.84	79.2	1.39	97	108	11	1.11	85	20	1.29	6.3	A+|Stb	Aa2|Stb
2046	01/27/2015	1.43	1.99	56.4	1.39	2.25	2.92	67.4	1.30	82	93	11	1.13	67	17	1.24	6.9	AA-|Neg	Aa2|Neg
2045	05/06/2013	1.80	2.47	66.9	1.37	2.72	3.49	76.7	1.28	92	102	10	1.11	71	13	1.01	7.5	AA-|Neg	Aa2|Stb
2043	01/25/2012	2.04	2.65	60.7	1.30	2.99	3.55	55.8	1.19	84	90	6	1.07	102	18	1.00	8.1	AA-|Stb	Aa1|Neg
2041	06/09/2010	3.35	3.76	40.7	1.12	4.24	4.67	42.6	1.10	89	91	2	1.02	-	34	1.04	8.4	AA-|Stb	Aa1|Stb
Summary	Average	1.72	2.23	50.5	1.38	2.55	3.13	58.0	1.26	81	90	9	1.11	73	19	1.19	7.4		
stats for	Median	1.72	2.11	53.8	1.33	2.43	2.93	59.8	1.23	83	91	10	1.12	67	18	1.26	7.2		
2041-2051	Min	0.58	1.10	24.4	1.12	1.31	1.95	33.4	1.10	61	71	2	1.02	54	10	1.00	5.3		
benchmarks	Max	3.35	3.76	67.7	1.88	4.24	4.67	79.2	1.49	97	108	13	1.17	102	34	1.35	10.6		

Notes: Levels for 2041 to 2050 benchmarks refer to prevailing market conditions on the day prior to launch of new Ontario 30-year benchmark; levels for 2052 WI refer to 22-Jul-2021; Ontario spreads refer to prior benchmark vs. corresponding GoC bond; jobless rate refers to SA average for month of bond issue (or latest); credit ratings & outlook refer to Ontario

Source: NBF, Bloomberg, StatCan, S&P, Moody's

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