Q. **Finance**

Provide the most current copies of all credit rating reports for Hydro, Nalcor and the Government of Newfoundland and Labrador.

A. As requested, please find attached copies of the latest credit ratings for:

- PUB-NLH-072, Attachment 1 – Newfoundland and Labrador Hydro as published by DBRS (October 4, 2016);
- PUB-NLH-072, Attachment 2 – Province of Newfoundland and Labrador as published by DBRS (July 14, 2017);
- PUB-NLH-072, Attachment 3 – Province of Newfoundland and Labrador as published by Moody's Investors Services (July 27, 2017);
- PUB-NLH-072, Attachment 4 – Province of Newfoundland and Labrador as published by Standard & Poor's (July 14, 2017). Reprinted with permission of Standard & Poor's Financial Services LLC, a wholly owned subsidiary of S&P Global Inc. Copyright@2017. All rights reserved.

Hydro has been advised that Nalcor Energy does not have a credit rating.

Rating Report

Newfoundland and Labrador Hydro

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Insight beyond the rating.

Ratings

Debt	Rating	Trend
Guaranteed Long-Term Debt (bsd. on Prov. Nfld)	A (low)	Stable
Guaranteed Short-Term Debt (bsd. on Prov. Nfld)	R-1 (low)	Stable

Rating Update

DBRS Limited (DBRS) has updated its report on Newfoundland and Labrador Hydro (Hydro or the Company). The ratings assigned to the Company's Guaranteed Long-Term Debt and Guaranteed Short-Term Debt are a flow-through of the ratings of the Province of Newfoundland and Labrador (the Province; rated A (low) and R-1 (low) with Stable trends by DBRS; see DBRS's press release on the Province dated April 15, 2016), which unconditionally guarantees all of Hydro's outstanding debt. The unconditional guarantee extends to principal, interest and, where applicable, sinking fund payments relating to the Company's promissory notes, debentures and long-term loans. Please see *DBRS Criteria: Guarantees and Other Forms of Support* for further detail. DBRS views Hydro as self-supporting as it is able to fund its own operations and service its debt.

Hydro continued to execute on its large capital expenditures (capex) program in 2015, spending approximately $163 million for the year. Although this was substantially lower than in 2014, following the installation of a 100 megawatt (MW) gas turbine at Holyrood Thermal Generating Station (Holyrood), capex is expected to ramp up in 2016 (forecast of $263 million) with the beginning of construction on a transmission line from Bay d'Espoir to Western Avalon (total capex of approximately $292 million). Furthermore, in its 2017 to 2021 capital plan submitted to the Board of Commissioners of Public Utilities (PUB), the Company plans to invest an average of $194 million over the five-year period, significantly higher than historical levels. As a result, the high capex is expected to result in a weakening in Hydro's key financial ratios for the near-term. DBRS notes, however, that leverage at the consolidated level remains reasonable, allowing for some financial flexibility during this period of significant capex. Additionally, with the decision for the general rate application (GRA) expected by the end of the year, the rate increase should result in higher earnings and cash flows for the Company going forward to help fund its capex program.

DBRS remains concerned with the potential for a large increase in electricity rates for the Province when the Muskrat Falls project, currently under construction by Nalcor Energy (100% owner of Hydro, and is in turn 100% owned by the Province), comes on line in 2019/2020. While it is currently uncertain how the cost of the project will be recovered from the Company's customers, should the potential upward pressure on rates affect the Company's ability to pass on costs, this could result in deterioration in Hydro's key financial ratios.

Financial Information

Newfoundland and Labrador Hydro

Consolidated	12 mos. to June 30	For the year ended December 31				
(CAD millions where applicable)	**2016**	**2015**	**2014**	**2013**	**2012**	**2011**
Total debt 1	1,018	1,095	1,072	902	923	893
Cash flow/Total debt 1	12.4%	11.2%	13.7%	14.2%	15.0%	16.9%
Total debt in capital structure 1	48.3%	51.1%	51.2%	46.1%	46.8%	47.1%
EBIT gross interest coverage (times)	1.67	1.63	1.89	1.60	1.66	1.86
Net income before non-recurring items	48	50	75	53	68	90
Cash flow from operations	126	123	147	128	138	151

1 Debt is net of sinking fund assets.

Issuer Description

Newfoundland and Labrador Hydro, a Crown corporation of the Province of Newfoundland and Labrador, generates, transmits and distributes electricity in the Province.

Rating Considerations

Strengths	Challenges

Strengths

1. Debt is guaranteed by the Province

The Province unconditionally guarantees Hydro's debt in exchange for an annual guarantee fee of 0.25% on obligations with maturities less than or equal to ten years and 0.5% on obligations with maturities greater than ten years (net of sinking funds), outstanding as of the preceding December 31. As a result, the ratings of Hydro are a flow-through of the Province's ratings.

2. Reasonable regulatory environment

The regulatory environment has contributed to a generally stable financial profile since 2002. The Province issued an Order in Council in 2009 for Hydro to earn a return on equity (ROE) equal to that of Newfoundland Power, effective at its next GRA. There have, however, been substantial delays in the GRA process — Hydro filed its GRA with the PUB in July 2013 for rates effective January 1, 2014, and subsequently filed an amended GRA in November 2014. Once approved, the new rates will reflect a ROE of 8.50%. While the GRA application remains on file, the PUB has approved (a) interim rates effective July 1, 2015, albeit at a level below the Company's request, and (b) the deferral of 2014 and 2015 costs to represent the effect of bringing rates in line with 2014 and 2015 cost levels, although the recovery of this amount will be subject to a future rate order.

3. Minimal competition

Geographic isolation and the lack of availability of natural gas minimize competitive pressures for the Company.

Challenges

1. Increased levels of planned capital expenditure

Hydro has significant planned capex over the medium term, including approximately $263 million for 2019. The Company plans to fund capital spending through internally generated cash flows and by issuing debt. The higher debt levels will likely pressure Hydro's financial profile for the medium term. This will be slightly mitigated by the higher cash flows and earnings for the Company after the GRA is approved.

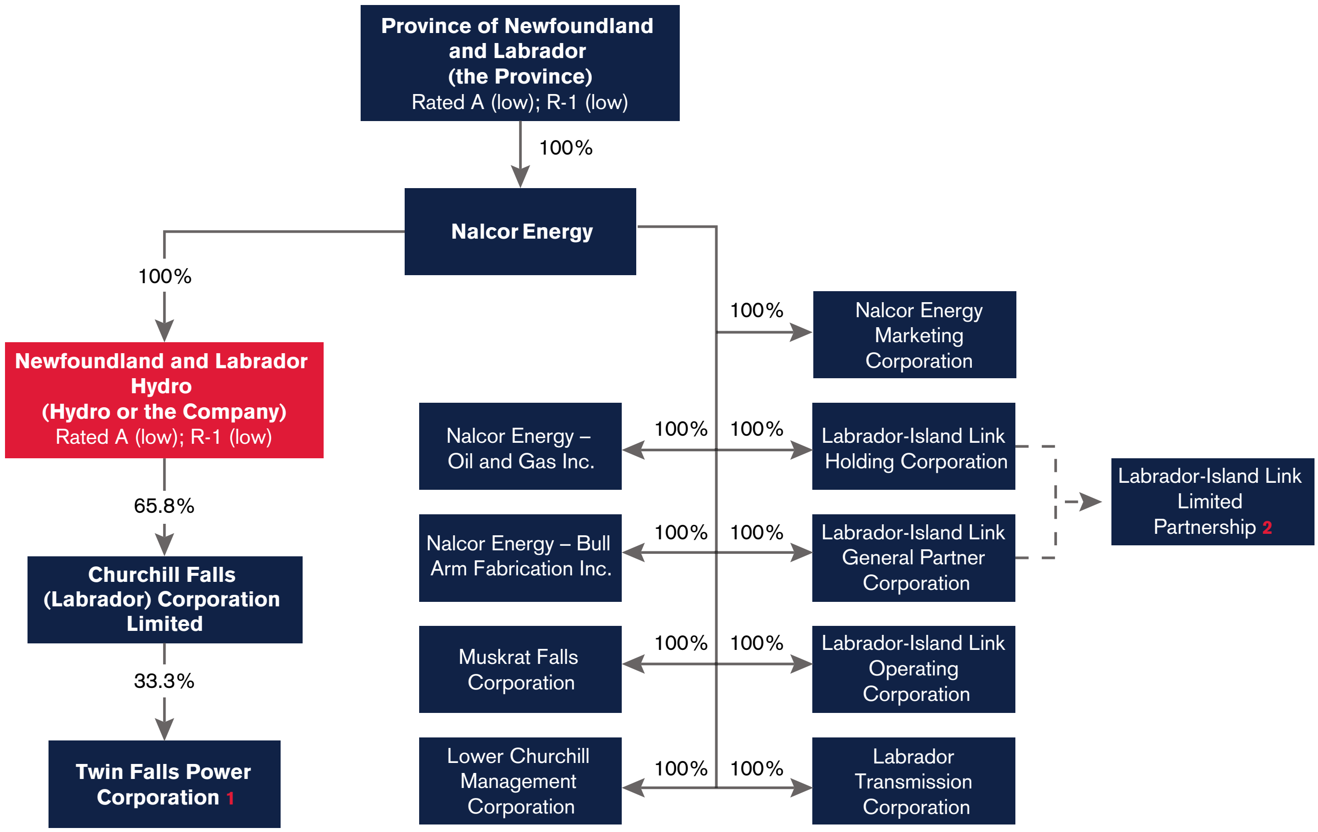
2. Sensitivity to weather

Demand for Hydro is correlated with the weather, which has a direct impact on annual earnings and cash flows.

3. Pressure on rates from the Muskrat Falls project

The Muskrat Falls project is an 824 MW hydroelectric generating facility being developed by Nalcor Energy. Costs for the project have increased to approximately $11.5 billion from $9.0 billion in September 2015. It is currently uncertain how costs for the project will be recovered from Hydro's customers; however, should upward pressure on rates affect the Company's ability to pass on costs, this would negatively affect its key financial ratios. Additionally, a potential rate shock for customers could affect their ability to pay their electricity bills as well as the electricity throughout, which would be negative for the Company's earnings and cash flows.

Simplified Corporate Structure



1 Shareholdings in Twin Falls Power Corporation consist of Class A and B shares. The issued Class A shares are entitled to four votes per share and the Class B are entitled to one vote per share. There are 250,000 Class A and 500,000 Class B shares issued and outstanding. Churchill Falls (Labrador) Corporation Limited is the holder of all Class A shares with the Class B shares held by other parties.

2 Labrador-Island Link Holding Corporation currently holds 65.0% while Emera Inc. holds 35.0% interest of the limited partnership in Labrador-Island Link Limited Partnership.

Company Profile

- Hydro is a Crown corporation owned by Nalcor Energy, which is in turn 100% owned by the Province.
- Hydro is the dominant electric generation and transmission power company in the Province. It also directly serves residential, commercial and industrial distribution customers in more rural service areas.
- The Company supplies over 90% of the Province's electrical energy. In 2015, it sold approximately 55% of its available supply to an investor-owned electricity distributor, Newfoundland Power, that is wholly owned by Fortis Inc. (rated A (low), Under Review with Negative Implications by DBRS). Hydro's remaining power deliveries are directed to its own distribution customers across the Province as well as six large industrial companies. Short-term exports of unused recall power from Churchill Falls (525 MW) are sold to other parties via the energy-marketing division.
- The Company's regulated operations have installed generating capacity of 1,762 MW, consisting of hydroelectric (956 MW), thermal (741 MW) and diesel (65 MW) power.
- Churchill Falls has installed generating capacity of 5,428 MW and a power contract with Hydro-Québec (rated A (high) with a Stable trend by DBRS) for the majority of the electricity generated from this facility (approximately 30 terawatt hours until 2041).
- Hydro has long-term supply contracts and power purchase arrangements with non-utility power producers in the Province.
- Upon completion of the Lower Churchill project, the Company will be the off-taker for a portion of Muskrat Falls' generating output and some of its transmission capacity via power purchase agreements.

Earnings and Outlook

Consolidated	12 mos. to June 30	For the year ended December 31				
(CAD millions where applicable)	2016	2015	2014	2013	2012	2011
Net sales	439	446	446	400	392	398
EBITDA	224	216	231	211	211	224
EBIT	141	138	162	145	150	168
Gross interest expense	85	85	86	91	91	91
Net income before non-recurring items	48	50	75	53	68	90
Reported net income	48	43	73	54	64	91
Return on equity	5.9%	6.2%	9.7%	7.1%	9.3%	12.7%
DBRS Adjusted Segment EBIT						
Hydro Regulated	97	79	109	98	112	112
Churchill Falls	37	41	18	22	19	13
Energy Marketing	9	20	38	32	19	46

2015 Summary

- Hydro's earnings are generated primarily from its regulated electricity generation, transmission and distribution business.
- Earnings decreased in 2015, largely because of weaker results from the regulated and energy marketing segment.
  - Earnings for the regulated segment decreased largely because of higher fuel costs compared to 2014, as the PUB did not approve for the deferral of diesel and gas turbine fuel for standby generation in excess of the test year amounts. The Company filed an application with the PUB in February 2016 to provide for the recovery of these amounts. The decrease was partly offset by interim rates approved for July 1, 2015.
  - The Energy Marketing segment saw lower earnings because of a decrease in average market prices for the year (USD 25.08/MWh in 2015, versus USD 38.80/MWh in 2014), as well as higher operating costs.
  - This was slightly offset by stronger performance for the Churchill Falls segment following a new power purchase agreement with Hydro effective January 2015, for the sale of up to 225 MW of energy produced by the Churchill Falls Generating Station.

2016 Summary/Outlook

- Earnings for the last 12 months (LTM) 2016 remained in line with 2015.
- While earnings for the regulated segment improved as a result of lower operating costs and the approval of interim rates effective July 1, 2015, this was offset by weaker Energy Marketing segment performance from the settlement of commodity hedges and lower export sales.
- A decision on Hydro's GRA application is expected by the end of 2016, which should help improve earnings going forward.
  - DBRS notes, however, that the PUB identified several disallowances in its prudence review of some of the Company's projects and operations. Hydro expects its 2014 and 2015 revenue requirement to be decreased by approximately $9 million as a result of the review.
- Earnings should also improve if the PUB approves the Company's application for a deferral account for fuel consumed by standby generators.
- Earnings volatility will continue to be managed through stabilizing the fuel prices and customer load variations in the Rate Stabilization Plan (RSP) by recovering from or refunding to customers in future rates.

Financial Profile and Outlook

Consolidated	12 mos. to June 30	For the year ended December 31				
(CAD millions where applicable)	2016	2015	2014	2013	2012	2011
Net income before non-recurring items	48	50	75	53	68	90
Depreciation & amortization	83	79	70	66	60	55
Deferred income taxes and other	(5)	(6)	2	9	10	6
Cash flow from operations	**126**	**123**	**147**	**128**	**138**	**151**
Dividends paid	(29)	(45)	(43)	(39)	(30)	(78)
Capital expenditures	(163)	(163)	(243)	(113)	(108)	(88)
Free cash flow (bef. working cap. changes)	**(65)**	**(84)**	**(139)**	**(24)**	**0**	**(15)**
Changes in non-cash work. cap. items	43	(2)	8	11	(63)	(18)
Rate stabilization/Regulatory adjustments	35	58	(66)	56	30	14
Net free cash flow	**12**	**(29)**	**(197)**	**43**	**(33)**	**(19)**
Acquisitions & investments	5	3	(3)	(0)	9	2
Proceeds on asset sales	1	1	3	4	4	5
Net equity change	0	0	0	2	0	0
Net debt change	6	44	84	(11)	52	0
Increase/Decrease in sinking fund	(8)	(8)	101	(28)	(26)	(25)
Other investing and financing	7	4	18	(3)	(10)	(1)
Change in cash	**23**	**15**	**7**	**7**	**(4)**	**(37)**
Total debt 1	1,018	1,095	1,072	902	923	893
Cash and equivalents	69	40	29	19	12	25
Cash flow/Total debt 1	12.4%	11.2%	13.7%	14.2%	15.0%	16.9%
Total debt in capital structure 1	48.3%	51.1%	51.2%	46.1%	46.8%	47.1%
EBIT interest coverage (times)	1.67	1.63	1.89	1.60	1.66	1.86
Dividend payout ratio	59.3%	89.8%	56.8%	72.8%	44.8%	87.1%

1 Debt is net of sinking fund assets.

2015 Summary

- Hydro's cash flow-to-debt and EBIT interest coverage decreased in 2015, as a result of the weaker earnings for the year. The Company's leverage remained stable for the year. Overall, the Company's key financial ratios continued to remain reasonable.
- Cash flow from operations were lower because of the weaker earnings for the year.
- Capex decreased significantly in 2015, as 2014 included $95 million on the supply and installation of a 100 MW combustion turbine generator at Holyrood.
- Hydro's dividend policy is: (1) based on maintaining the regulated segment's target capital structure at 75% debt and (2) paying out excess cash from the sale of recall power for the non-regulated segments.
- The Company's net free cash flow deficit was funded with short-term promissory notes.

2016 Summary/Outlook

- Hydro's key financial ratios improved modestly in LTM 2016 because of the lower level of debt (net of sinking fund assets).
- The Company has forecast capex of approximately $263 million for 2016. This amount includes around $224 million for the regulated segment, with (1) $183 million representing the 2016 capital budget as approved by the PUB in December 2015 (that includes $75 million for the construction of a transmission line from Bay d'Espoir to Western Avalon) and (2) $18 million for additional work at Holyrood.
- Hydro expects to fund the capex through internally generated operating cash flow and debt. Dividends are expected to be restricted for the medium term as the Company undergoes this period of significant capex.

Long-Term Debt Maturities and Bank Lines

- Promissory notes, debentures and long-term loans are unsecured and unconditionally guaranteed as to principal and interest and, where applicable, sinking fund payments by the Province. The Province charges a guarantee fee of 0.25% and 0.5% annually on obligations with maturities less than or equal to ten years and greater than ten years, respectively (net of sinking funds), outstanding as of the preceding December 31.
- Hydro has a $300 million short-term promissory note program, guaranteed by the Province, that it uses for its daily funding requirements. As at June 30, 2016, the Company had $34 million (at par) outstanding.
- Hydro has a $50 million unsecured operating credit facility with a commercial bank that is used primarily to backstop the Company's short-term promissory note program and to support letters of credit. As at June 30, 2016, there was no amount outstanding on the operating line of credit, however, one letter of credit was outstanding that reduced available credit by $0.3 million.

(CAD millions)	2016	2017*	2018	2019	2020	Thereafter	Total
As at June 30, 2016	0	150	0	0	0	1,146	1,296
	0%	12%	0%	0%	0%	88%	100%

Note: Includes term debt maturities and sinking fund requirmenets for Hydro only.
* Includes $150 million of Notes to be repaid from the sinking fund reserve.

- The debt maturity profile is well distributed, with only 12% of total debt due in 2017.

Regulation

- The Company is regulated by the PUB based on a return on rate base model under cost of service regulation.
- Hydro has a RSP that provides for the deferral of cost variances resulting from changes in fuel prices relative to the base price, levels of precipitation and load.
  - Accumulated balances related to fuel cost variations will be recovered over the following one-year period.
  - Accumulated balances related to variations in hydrology will be recovered at a rate of 25% of the outstanding balance at year-end, including the weighted-average cost of capital on the balance.
  - The RSP allows Hydro to smooth out the rate increases required to recover the cost variances.
- The 2006 GRA established a return on rate base of 7.44%, based on an allowed ROE of 4.47%.
- Hydro filed a GRA with the PUB in July 2013, requesting new rates effective January 1, 2014. As a result of significant delays in the GRA process, the Company filed an amended GRA in November 2014, based on 2014 and 2015 test years. A decision on the application is expected by the end of 2016.
- Once approved by the PUB, new rates will reflect an ROE of 8.80%, equal to that of Newfoundland Power. Hydro has applied for a return on rate base of 7.12% and rate base of $1,692.6 million for 2014, and a return on rate base of 6.82% and rate base of $1,802 million for 2015.
  - Newfoundland Power's allowed ROE was subsequently reduced to 8.50% for 2016.
- The Company has an internal target debt-to-equity ratio of 75:25 for regulated operations. After approval of the amended GRA, Hydro will be entitled to have equity in its capital structure up to the same amount as Newfoundland Power (currently 45% equity with 55% debt). However, Hydro expects to maintain its target of 75% debt.
- On January 28, 2015, the Company filed an application with the PUB for interim rates effective March 1, 2015. The PUB approved certain aspects of the application for rates effective July 1, 2015. Hydro has forecast a deficiency of approximately $44 million in profit for 2015, largely as a result of the later implementation date. Consequently, the Company filed an application for 2015 cost deferral of $20 million in July 2015 that was subsequently amended in November 2015 to $60 million.
  - In December 2015, the PUB approved a cost deferral of $30 million for 2015. The deferral of 2015 supply costs related to fuel consumed in combustion turbines and diesel generators was not approved.
  - Hydro filed an application for a deferral account for those fuel types in February 2016.
- The PUB approved a $76.8 million capital budget for 2015 in December 2014. The PUB also approved the Company's capital budget of $184 million in December 2015.
- In January 2015, the PUB began conducting a prudence review of certain Hydro expenditures. The PUB determined that some costs related to projects done by the Company and the 2013, 2014 and 2015 outages were imprudent and the Company will not be allowed to recover them.
  - Hydro filed its compliance application to the PUB in May 2016, reducing its 2014 test year revenue requirement by $6 million and its 2015 test year requirement by $3 million.

Newfoundland and Labrador Hydro (Consolidated)

Balance Sheet	June 30	December 31			June 30	December 31	
(CAD millions)	**2016**	**2015**	**2014**		**2016**	**2015**	**2014**
Assets				**Liabilities & Equity**			
Cash & equivalents	69	40	29	S.T. borrowings	34	97	53
Accounts receivable	63	109	105	Accounts payable	144	133	151
Inventories	77	78	97	Current portion L.T.D.	233	233	8
Prepaid expenses & other	38	69	9	Other current liab.	24	63	2
Total current assets	**246**	**296**	**239**	**Total current liab.**	**435**	**526**	**214**
Net fixed assets	2,135	2,109	2,030	Long-term debt	1,006	1,007	1,239
Sinking funds	256	243	228	Provisions	152	149	156
Regulatory assets	138	144	124	Regulatory liabilities	375	330	252
Investments & others	40	40	44	Other L.T. liab.	12	12	12
				Shareholders' equity	834	806	792
Total assets	**2,816**	**2,831**	**2,666**	**Total liab. & SE**	**2,816**	**2,831**	**2,666**

Balance Sheet & Liquidity & Capital Ratios (Consolidated)	12 mos. to June 30	For the year ended December 31				
	2016	**2015**	**2014**	**2013**	**2012**	**2011**
Current ratio	0.57	0.56	1.12	0.59	0.56	0.64
Total debt in capital structure 1	48.3%	51.1%	51.2%	46.1%	46.8%	47.1%
Cash flow/Total debt 1	12.4%	11.2%	13.7%	14.2%	15.0%	16.9%
(Cash flow-dividends)/Capex (times)	0.60	0.48	0.43	0.79	1.00	0.83
Dividend payout ratio	59.3%	89.8%	56.8%	72.8%	44.8%	87.1%
Coverage Ratios (times)						
EBIT interest coverage	1.67	1.63	1.89	1.60	1.66	1.86
EBITDA interest coverage	2.64	2.56	2.71	2.33	2.33	2.47
Fixed-charges coverage	1.67	1.63	1.89	1.60	1.66	1.86
Operating Efficiency						
Power purchases/Revenues	13.1%	13.0%	9.8%	10.2%	10.4%	9.0%
Fuel costs/Revenues	23.1%	25.3%	38.5%	30.9%	31.2%	26.5%
Profitability Ratios						
EBITDA margin	50.9%	48.5%	51.8%	52.8%	53.8%	56.1%
EBIT margin	32.1%	30.8%	36.2%	36.3%	38.4%	42.2%
Profit margin	11.0%	11.2%	16.9%	13.4%	17.3%	22.5%
Return on equity	5.9%	6.2%	9.7%	7.1%	9.3%	12.7%
Return on capital	6.2%	6.2%	7.8%	7.3%	8.2%	9.7%

1 Debt is net of sinking fund assets.

Operating Statistics

	For the year ended December 31				
Electricity sold – breakdown	**2015**	**2014**	**2013**	**2012**	**2011**
Utilities (Newfoundland Power)	6,072	5,852	5,606	5,359	5,317
Rural	1,092	1,089	1,017	998	949
Industrial*	2,231	535	559	607	491
Exports	1,645	1,545	1,514	1,559	1,594
Total (GWh sold)	**11,040**	**9,021**	**8,696**	**8,523**	**8,351**
Energy sales growth	22.4%	3.7%	2.0%	2.1%	3.3%
Generating capacity (MW)					
Hydroelectric	956	956	939	939	939
Thermal (Oil)	741	617	617	617	632
Diesel	65	64	53	52	55
Installed capacity	1,762	1,637	1,609	1,608	1,626
Electricity generated and purchased (GWh)					
Electricity Generated – hydroelectric	4,823	4,658	4,688	4,595	4,512
Electricity Generated – thermal	1,500	1,316	956	851	873
Electricity Generated – diesel	52	54	49	45	49
Gross energy generated	**6,375**	**6,028**	**5,693**	**5,491**	**5,434**
Plus: purchases*	5,126	3,339	3,408	3,395	3,305
Energy generated + purchased	**11,501**	**9,367**	**9,101**	**8,886**	**8,739**
Less: transmission losses + internal use	461	346	405	364	386
Total sales	**11,040**	**9,021**	**8,696**	**8,522**	**8,353**
Energy lost/energy gen + purch.	4.0%	3.7%	4.5%	4.1%	4.4%
Maximum Island Interconnected peak demand	1,550	1,535	1,501	1,385	1,399
Peak Island Interconnected demand/available capacity	88.0%	93.8%	93.3%	86.1%	86.0%

* Total purchases and sales for 2015 include the former Twinco Block following the expiration of the Twinco arrangements on December 31, 2014.

Rating History

	Current	2015	2014	2013	2012	2011
Guaranteed Long-Term Debt (bsd. on Prov. Nfld)	A (low)	A	A	A	A	A
Guaranteed Short-Term Debt (bsd. on Prov. Nfld)	R-1 (low)	R-1 (low)	R-1 (low)	R-1 (low)	R-1 (low)	R-1 (low)

Previous Action

- Downgraded, April 15, 2016.

Related Research

- Newfoundland and Labrador, Province of: Rating Report: November 19, 2015.

Previous Report

- Newfoundland and Labrador Hydro, Rating Report: September 16, 2015.

Notes:
All figures are in Canadian dollars unless otherwise noted.

For the definition of Issuer Rating, please refer to Rating Definitions under Rating Policy on **www.dbrs.com**.

Generally, Issuer Ratings apply to all senior unsecured obligations of an applicable issuer, except when an issuer has a significant or unique level of secured debt.

Rating Report

Province of Newfoundland and Labrador

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DBRS

Insight beyond the rating

Ratings

Debt	Rating	Rating Action	Trend
Issuer Rating	A (low)	Confirmed	Stable
Long-Term Debt *	A (low)	Confirmed	Stable
Short-Term Debt *	R-1 (low)	Confirmed	Stable

* Includes guaranteed debt issued by Newfoundland and Labrador Hydro and Newfoundland and Labrador Municipal Financing Corporation

Rating Update

DBRS Limited (DBRS) has confirmed the Issuer Rating of the Province of Newfoundland and Labrador (Newfoundland or the Province) at A (low), as well as its Long-Term Debt and Short-Term Debt ratings at A (low) and R-1 (low), respectively. All trends remain Stable. The ratings confirmation reflects DBRS's view that the considerable progress being made to reduce budgetary deficits and slow debt growth are sufficient to maintain financial metrics within an acceptable range for the current ratings. An uncertain outlook for global commodity prices and continued cost overruns at the Muskrat Falls hydroelectric project present downside risks.

Preliminary results show the Province recorded a better-than-expected deficit of $1.1 billion in 2016–17. On a DBRS-adjusted basis, this equates to a shortfall of $1.6 billion, or 5.3% of gross domestic product (GDP). Total revenues are estimated to have grown sharply by 22.7% with the introduction of significant tax increases and a partial recovery in offshore oil royalties. The unexpected incremental offshore oil revenue enabled the Province to outperform its budget target. This contained debt growth to 4.0%, resulting in a debt-to-GDP ratio of 50.4%, up from 48.2% in 2015–16.

For 2017–18, the budget forecasts a deficit of $778 million, which equates to a DBRS-adjusted shortfall of $982 million, or 3.2% of GDP. Following last year's extensive tax increases, no further increases were announced, and total revenues are forecast to be relatively flat. However, the Province continues to move forward with expenditure restraint measures aimed at bringing the level of per capita spending in line with the average of its Atlantic Canadian peers. As a result, total DBRS-adjusted spending is budgeted to decline by 6.8% in 2017–18.

Over the medium term, the Province's plan points to a steadily declining deficit until balance is achieved in 2022–23, which suggests DBRS-adjusted debt will reach approximately 55% of GDP in 2018–19 before potentially declining slowly thereafter. This marks a considerable improvement from the potential peak debt burden of 65% of GDP foreseen at the time of DBRS's last review and remains within an acceptable range for the current ratings. However, this outlook remains subject to downside risks, including the Province's ability and willingness to meet fiscal plan targets and the rising costs at Muskrat Falls, which may need to be partly borne by the tax base.

For 2017, the Province has assumed that the economy will contract by 3.8% in real terms. This compares with the current private sector consensus tracked by DBRS, which shows a more modest 2.0% contraction. For 2018, the Province forecasts a

Continued on P. 2

Financial Information

(all financial figures DBRS adjusted)	For the year ended March 31 2017-18B	2016-17P	2015-16	2014-15	2013-14
Debt*/GDP 1	54.3%	50.4%	48.2%	31.3%	28.2%
Surplus (deficit)/GDP 1	(3.2%)	(5.3%)	(7.8%)	(3.8%)	(2.0%)
Federal transfers/total revenues	17.3%	16.8%	17.9%	14.7%	13.7%
Interest costs/total revenues	14.4%	14.5%	15.6%	10.4%	10.7%
Real GDP growth 1	(3.8%)	(0.7%)	(2.0%)	(1.0%)	5.2%

* DBRS-defined: tax-supported debt + unfunded pension liabilities. B = Budget. P = Projected. 1 GDP based on calendar years ending December 31.
Sources: Province of Newfoundland and Labrador, Statistics Canada and DBRS calculations.

Issuer Description

Newfoundland and Labrador is the eastern-most province in Canada and is heavily reliant on natural resources, particularly oil, iron ore and nickel. Among Canadian provinces, Newfoundland ranks ninth by nominal GDP and population.

Rating Update (CONTINUED)

further contraction in real GDP of 0.2%, with little improvement anticipated through the remainder of the forecast horizon to 2021. A continued moderation in capital investment, ongoing fiscal constraint and weak demographics will do little to stimulate growth.

A negative rating action could result from a sustained deterioration in budgetary performance and material increase in debt beyond that considered acceptable for an "A"-range province. A positive rating action is unlikely in the current environment.

Rating Considerations

Strengths

1. Significant energy resources
Development of the Province's substantial offshore oil resources has had a dramatic impact on the economy. Output at the three projects currently in production – Hibernia, Terra Nova and White Rose – peaked in 2007, as these fields are now in the mature stages of their lifecycle; however, the Hebron platform, being used for the second-largest discovery to date after Hibernia, was recently towed to sea, with first oil expected in late 2017. There have been several significant discoveries in recent years, including Harpoon, Bay du Nord and Mizzen, which could be developed once economically feasible, and further exploration activity is underway.

2. Commitment to restoring fiscal discipline
Since being elected in November 2015, the Liberal government has continued to emphasize the importance of fiscal consolidation in the wake of the rapid decline in commodity prices. The government presented a detailed multi-year plan to return to balance, which includes significant tax increases and measures to slow spending growth. Maintaining this discipline could become increasingly challenging as the government progresses through its mandate, and the public appetite for austerity fades.

3. Low reliance on federal transfers
Since 2011–12, Newfoundland has not received any equalization or offshore accord payments, which has greatly reduced its reliance on federal transfers. In 2016–17, federal transfers accounted for just 16.8% of total revenues – the lowest proportion outside of Western Canada. However, should low oil prices persist and Newfoundland's fiscal performance remain depressed relative to provincial peers, DBRS believes that Newfoundland could return to the ranks of equalization-receiving provinces over the medium to longer term.

Challenges

1. Reliance on volatile non-renewable resource sector
The Province's economic and fiscal performance are heavily dependent on the resource sector, with resource royalties directly accounting for between 10% and 36% of government revenue over the last six years. This figure does not include a meaningful amount of other revenue indirectly derived from related activities. Such dependence complicates the budgeting process, as a large portion of revenue is subject to volatile oil prices and production levels, which may be affected by a number of unpredictable factors. The Province estimates that a USD 1 per barrel change in the price of oil could affect revenues by approximately $22 million.

2. Rising debt burden
On a DBRS-adjusted basis, Newfoundland's debt burden rose to 50.4% of GDP in 2016–17, up from a low of 27.4% of GDP just five years earlier. This leaves Newfoundland with the second-highest debt burden of all provinces, which is now expected to peak around 55% of GDP in 2018–19. However, given the long path to fiscal recovery, ongoing cost overruns for the Muskrat Falls Hydroelectric project and uncertainty as to whether or not a portion of these costs will need to be included in tax-supported debt, the ultimate peak in debt remains unclear.

3. Renewal of public-sector labour agreements
Achievement of fiscal targets will depend, in part, on the successful renewal of public-sector labour agreements, many of which are in negotiations at present. The medium-term plan contemplates no increases in program spending over the forecast horizon, leaving no room for compensation increases. A 1.0% wage increase across the broader public sector is estimated to cost roughly $33 million.

4. Cost overruns at Muskrat Falls
Based on the latest cost estimates released in June 2017, development of the Muskrat Falls hydroelectric project is now expected to cost $12.7 billion, including financing costs, up from $7.4 billion when the project was sanctioned in 2012. An additional federal loan guarantee for $2.9 billion, on top of $5.0 billion already provided, has significantly reduced the required equity contribution from the Province; however, the impact of these cost overruns on future electricity rates has been significant. Nalcor Energy estimates that electricity rates could be 23 cents per kilowatt hour in 2022 when Muskrat Falls comes online, considerably above that expected in any other Province. This is likely to create significant political pressure to subsidize rates, or potentially shift a portion of the costs back to the tax base, which could materially boost tax-supported debt.

5. Weak demographics
The median age in Newfoundland was 45.3 years in 2016, which is the highest of all provinces and has been rising for many years. This will affect future demand for the health-care system and is contributing to a shrinking labour force as individuals transition to retirement. Population growth has been weak over the last five years, which is likely to limit Newfoundland's long-term economic growth potential, absent material productivity gains.

2017–18 Budget

Exhibit 1: DBRS-Adjusted Surplus (Deficit)-to-GDP

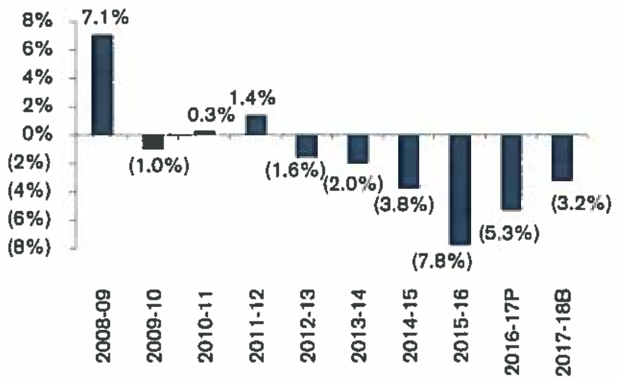
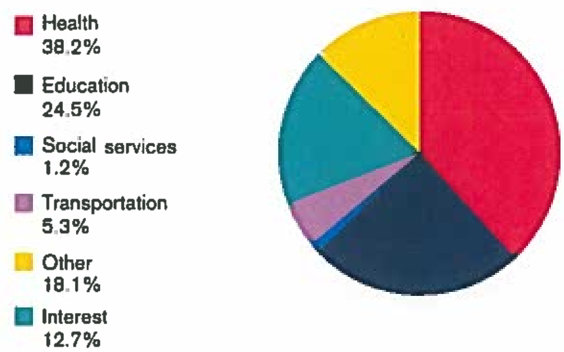


Exhibit 2: 2017–18 DBRS-Adjusted Expenditures
(Total: $8.3 billion)



Sources: Province of Newfoundland and Labrador and DBRS calculations

Newfoundland continues to demonstrate progress toward its objective of restoring balance, now expected by 2022–23. The 2017 budget forecasts a deficit of $778 million. On a DBRS-adjusted basis, this equates to a shortfall of $982 million, or 3.2% of GDP – much improved from $1.6 billion a year earlier.

Following last year's extensive tax increases, no further increases were announced in the 2017 budget. Total revenues are forecast to be relatively flat in 2017–18 and are based on very modest growth in nominal GDP of 1.8%. Tax revenues are projected to advance by 6.2% and largely reflect the full-year impact of measures announced last year, including a two-percentage-point increase in the harmonized sales tax, along with corporate income tax and personal income tax increases. Some modest tax relief will provide a partial offset, as the government announced plans to gradually unwind the temporary gas tax, lowering it by 8.5 cents per litre on June 1, 2017, and another 4.0 cents per litre on December 1, 2017. Mining and offshore royalties are based on an improved Brent Crude oil price assumption of USD 56 per barrel but are nevertheless forecast to fall by 9.8% based on lower oil production. Fiscal YTD, Brent Crude oil has averaged below USD 51 per barrel, and the Province estimates that a USD 1 per barrel change in the price of oil could affect revenues by approximately $22 million. A lower-than-budgeted exchange rate will partially offset soft YTD prices. Federal transfers are projected to rise by 2.7%, based on limited growth in health and social transfers (as Newfoundland accounts for a declining share of the national population) and modest growth in funding for other cost-shared programs.

The Province continues to move forward with expenditure restraint measures aimed at bringing the level of per capita spending in line with the average of Atlantic Canadian peers. As a result, total DBRS-adjusted spending is budgeted to decline by 6.8% in 2017–18. Key initiatives for the current year include a move to zero-based budgeting model, elimination of management positions, savings and efficiencies identified at government agencies and broader public sector entities, annualized savings from measures implemented the prior year and savings realized from actuarial and accrual adjustments (primarily related to pensions and non-pension benefits). The government has also announced a wage freeze for all management and non-union employees, including those of agencies, boards and commissions, which sets an example for upcoming labour negotiations. The majority of Newfoundland's collective agreements are up for renewal, and active discussions are underway, but with no budget provisions for wage increases, holding wages flat will test fiscal resolve and presents a key risk to the expenditure outlook. No program is being insulated from expenditure restraint, as health is only expected to receive a 0.2% increase, while education spending is being reduced by 3.0%. Gross capital spending, including capital grants, is budgeted to fall by $234 million, or 17.8%, which will help to slow debt growth. Interest expense, net of sinking fund earnings, is projected to remain flat, as the borrowing program is very modest.

Outlook

The 2017 budget takes another significant step forward in the Province's goal to restore fiscal balance. The medium-term plan points to a steadily declining deficit until balance is achieved in 2022–23. On a DBRS-adjusted basis, this equates to deficits of 2.5% of GDP in 2018–19 and slowly approaching zero by the end of the planning horizon. The plan is based on average annual revenue growth of 2.4% (DBRS-adjusted), assuming gradually rising oil prices and no increase in total spending. While DBRS recognizes the significant progress made thus far, the expenditure outlook remains aggressive and subject to downside risks and is, in part, reliant on the outcome of labour negotiations currently underway. An inability to hold spending flat may require the Province to revisit revenue measures or risk enduring longer deficits and rising debt.

2016–17 Preliminary Results

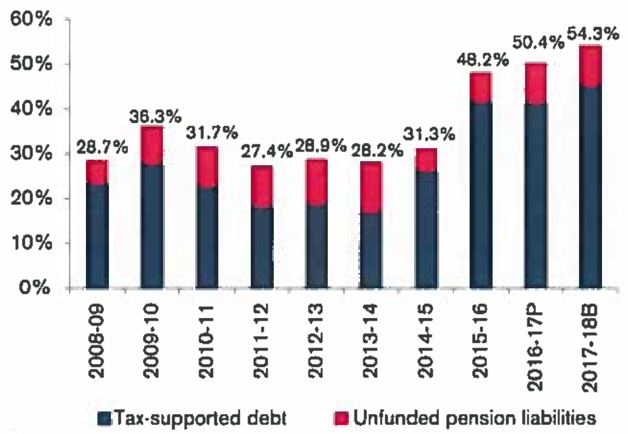
For the fiscal year ended March 31, 2017, preliminary results show the Province recorded a deficit of $1.1 billion compared with a budgeted deficit of $1.8 billion. On a DBRS-adjusted basis, this equates to a shortfall of $1.6 billion, or 5.3% of GDP. This represents the largest shortfall among Canadian provinces, although it is notably reduced from the 7.8% of GDP shortfall realized in 2015–16.

Total revenues are estimated to have grown sharply by 22.7% in 2016–17, well ahead of budget expectations. On a year-over-year (YOY) basis, growth was driven by a combination of substantive tax increases, increased offshore royalties and federal transfers. Tax receipts grew by 16.1% and largely reflected the government's decision to (1) raise the harmonized sales tax by two percentage points beginning July 1, 2016; (2) increasing personal income tax rates for all income brackets beginning July 1, 2016; (3) temporarily increasing the gasoline tax; (4) implementing an income-tested temporary deficit reduction levy; (5) re-introducing a tax on insurance premiums; (6) increasing financial corporations' capital tax, general corporate income tax and insurance companies' tax by one percentage point each; and (7) increasing tobacco taxes. In addition, offshore royalties grew by $448 million on account of increased oil production at Hibernia satellite fields that was only partially offset by lower prices. Federal transfers grew by 15.5% YOY as a result of legislated increases in health and social transfer envelopes as well as increased federal infrastructure funding. Relative to budget, the improvement was largely a result of higher-than-expected oil prices and production, which boosted offshore royalties.

DBRS-adjusted spending is estimated to have grown by 7.2% in 2016–17, although this primarily reflects higher-than-planned capital spending largely related to increased federal infrastructure funding, as most other program expenses were held below budget. Efforts to find efficiencies in program delivery costs resulted in $121 million in savings relative to 2015–16. Health-care spending contracted by 0.9%, though it still exceeded budget expectations based on volume and cost pressures, while education spending was held flat. No major labour agreements were settled during the year, although several expired and began active negotiations, which kept labour costs relatively stable. The acquisition of tangible capital assets grew by more than 80% YOY and was well ahead of budget expectations because of increased federal funding. Interest charges, net of sinking fund income, grew by 14.1% on account of a notable rise in debt. This was above expectations, largely because of pre-borrowing for future years.

Debt Profile

Exhibit 3: DBRS-Adjusted Debt-to-GDP



Following the decline in oil prices in 2014 and subsequent deterioration in fiscal performance, Newfoundland's debt rose sharply. However, the government has taken significant steps to contain the deficit, which have helped to meaningfully slow the pace of debt growth. After adjusting for pre-borrowing of $1.2 billion, DBRS-adjusted debt (defined as tax-supported debt plus unfunded pension liabilities) grew by $576 million, or 4.0% in 2016–17, considerably slower than the prior year. This resulted in the debt-to-GDP ratio rising to 50.4% as of March 31, 2017, up from 48.2% a year earlier. This was a better result than anticipated at the time of DBRS's last review, helped by improved fiscal performance and reduced equity contributions required for the Muskrat Falls project as a result of the federal loan guarantee. This leaves Newfoundland with the second-highest debt burden of all provinces.

After difficultly in 2015–16, Newfoundland continues to rebuild confidence in its finances and execute its borrowing strategy. In 2016–17, Newfoundland completed $2.9 billion in borrowing, including $1.2 billion in pre-borrowing, as actual cash requirements were significantly lower than expected at $1.7 billion. All borrowing was completed in the domestic market with an average term of 22.2 years. The debt structure remains prudent, with a well-laddered maturity profile wherein only 22.8% of gross direct debt matures over the next five years. In addition, unhedged foreign currency debt amounted to 5.7% of direct debt at March 31, 2017, while floating-rate debt has been reduced to a very manageable 6.5% of direct debt at March 31, 2017, down from more than 20.0% a year earlier.

The Province sponsors five defined-benefit pension plans, including the Public Service Pension Plan (PSPP), the Teachers' Pension Plan (TPP) and three smaller plans. In March 2015, the PSPP was converted to a joint trusteeship structure, whereby

Debt Profile (CONTINUED)

future actuarial deficits or surpluses will be shared equally by the Province and plan members rather than being the sole responsibility of the Province. In addition, other key changes to the plan included increased contribution rates, a change in the benefit calculation formula to the best six years' earnings rather than the best five years' earnings, lengthened retirement ages for early retirees and a suspension of benefit indexation for future service. In 2015–16, the TPP was also converted to a joint trusteeship structure, which provides for equal sharing of plan surpluses and deficits between the Province and plan members. In addition, changes were made to increase member contribution rates, suspend indexing and change the average pensionable earnings formula. In exchange for the concessions, the government agreed to provide promissory notes in the amount of $2.685 billion to the PSPP and $1.862 billion to the TPP, both to be amortized gradually over 30 years. The end result has been reduced unfunded pension liabilities in exchange for increased tax-supported debt obligations. DBRS notes, however, that the structural changes made to the plans should help to provide stability to annual pension contributions and minimize potential growth in unfunded pension liabilities going forward.

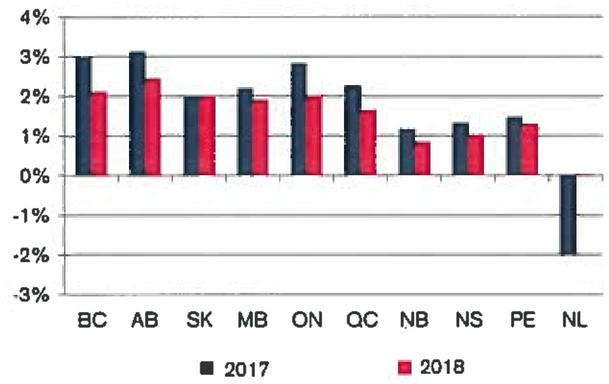
Outlook

For 2017–18, DBRS-adjusted debt is projected to grow by $1.5 billion, or 9.7%. When combined with expectations for modest growth in nominal GDP, this points to a debt burden of 54.3% of GDP. Gross cash requirements are forecast at $1.7 billion and are expected to be funded through a very modest borrowing program of $400 million (excluding the needs of Newfoundland and Labrador Hydro) and drawdown of cash from pre-borrowing last year of $1.2 billion. At the time of writing, no borrowing had been completed.

Over the medium term, based on the Province's fiscal recovery and multi-year capital plans and assuming no change in unfunded pension liabilities, annual debt growth is projected to slow to 3% or less between 2019–20 and 2022–23. As nominal GDP is expected to grow modestly, this points to the debt burden's stabilizing around 55% of GDP in 2018–19 and potentially declining slowly thereafter. This marks a considerable improvement from the potential peak debt burden of 65% of GDP foreseen at the time of DBRS's last review and remains within an acceptable range for the current ratings. DBRS notes that this outlook remains subject to downside risks, including the assumption that oil prices will continue to rise and that the full cost of the Muskrat Falls project will be recovered through electricity rates. However, the progress made thus far provides some flexibility to absorb higher debt levels should some of the risks materialize.

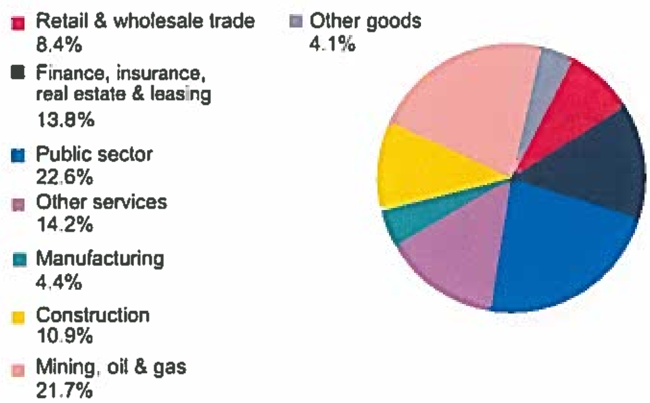
Economy

Exhibit 4: Real GDP Growth Outlooks*



* Based on major Canadian banks' forecasts at the time of this report.

Exhibit 5: 2015 GDP Breakdown**



** Statistics Canada, CANSIM 379-0028; figures may not add up because of rounding

Newfoundland's economy is undergoing a significant period of adjustment; the rapid decline in commodity prices and attendant decline in capital investment are both taking their toll. This adjustment is expected to take several years and is likely to affect all areas of the economy, presenting a challenge for government to navigate.

At budget time, the Province estimated that real GDP fell by 0.7% in 2016, although recent estimates by Statistics Canada point to an increase in real GDP by 1.9%, with the difference partially attributable to different measures of calculating GDP (expenditure versus industry). After several years of strong growth, capital investment has begun to moderate from the highs reached in 2015 as several large projects move closer to completion, including the Hebron offshore oil project and Vale's Long Harbour nickel processing plant. Increased oil output from the Hibernia field boosted oil production by 22.5% and was supportive of modest growth in overall provincial exports. Employment fell by 1.5%, pushing the unemployment rate to 13.4%, up from 12.8% in 2015. Weakness was primarily experienced in the manufacturing, mining, oil and gas, construction and forestry sectors, while service sector employment saw a slight increase. Newfoundland's population continued to expand, albeit by a modest 0.3%, driven entirely by international immigration. However, a weak labour market weighed on residential investment, as housing starts fell by 17.6% to approximately 1,400 units – the lowest level in 17 years. Not surprisingly, retail trade was relatively flat, as weak economic conditions and government restraint weighed on consumer sentiment.

Outlook

For 2017, the Province has projected that the economy will contract by 3.8% in real terms. This compares with the current private sector consensus tracked by DBRS showing a more modest 2.0% contraction. Falling capital investment will be a key contributor to the decline as Statistics Canada's survey of investment intentions points to a 17.7% drop in non-residential construction, machinery and equipment spending. Large capex projects such as Hebron, Vale's nickel processing facility and Muskrat Falls continue to move past peak construction and closer to production phases. Importantly, some large scale projects continue to move forward, including construction of the underground nickel mine at Voisey's Bay, and in May 2017, Husky sanctioned development of the West White Rose expansion project, which is estimated to cost approximately $2.2 billion and could add 15 to 20 years of production life to the White Rose offshore oil field. The West White Rose expansion project presents some modest upside to the Province's growth forecast, as it was not fully incorporated at the time of the budget. Furthermore, while oil production was expected to decline, production is up through the first four months of the year, which partly explains the more optimistic private-sector forecast. Employment is expected to fall by 1.9%, pushing the unemployment rate up to 13.9%. As of June 2017, the unemployment rate already stood at 14.9% (seasonally adjusted), which is the highest of all provinces. Weak labour markets are expected to dampen international immigration, with the population forecast to contract by 0.5%. The overhang from last year's tax increases is also weighing on domestic activity, as housing starts are expected to fall even further, and retail sales growth only advanced by 1.0% YTD as of April 2017.

For 2018, the Province forecasts a further contraction in real GDP of 0.2%, with little improvement anticipated through the remainder of the forecast horizon to 2021. A continued moderation in capital investment, ongoing fiscal restraint and weak demographics will do little to stimulate growth. In the near term, the outlook for commodity prices and protectionist trade talk present downside risks. Over the longer term, the offshore energy sector continues to boast considerable potential, but any future development will be subject to confidence around the future direction of oil prices and could take many years to materialize.

Economic Statistics

	For the year ended December 31						
	2018P	**2017P**	**2016**	**2015**	**2014**	**2013**	**2012**
Nominal GDP ($ millions)	31,486	30,503	29,967	30,100	34,022	34,462	32,032
Nominal GDP growth	3.2%	1.8%	(0.4%)	(11.5%)	(1.3%)	7.6%	(4.5%)
Real GDP growth	(0.2%)	(3.8%)	(0.7%)	(2.0%)	(1.0%)	5.2%	(4.4%)
Population (thousands)	525.0	527.3	530.1	528.7	528.3	527.4	526.5
Population growth	(0.4%)	(0.5%)	0.3%	0.1%	0.2%	0.2%	0.3%
Employment (thousands) (annual average)	221.8	228.3	232.6	236.2	238.6	242.7	240.8
Unemployment rate	15.5%	13.9%	13.4%	12.8%	11.9%	11.6%	12.3%
Housing starts (units)	1,251	1,350	1,398	1,697	2,119	2,862	3,885
Retail sales ($ millions)	8,844	8,970	8,988	8,972	8,919	8,606	8,187
Inflation rate (CPI)	2.4%	2.9%	2.7%	0.5%	1.9%	1.7%	2.1%
Primary Household income per capita ($)	36,372	36,359	36,274	36,120	34,984	33,666	31,878

Source Statistics Canada (actuals) Province of Newfoundland and Labrador (Budget 2017) projections P = Projected.

Budget Summary

($ millions)	Budget 2017-18	2016-17	Budget 2016-17	2015-16	2014-15	2013-14
Revenue (DBRS adjusted)	7,278	7,264	6,722	5,918	6,866	7,432
Program expenditure (DBRS adjusted)	(7,209)	(7,805)	(7,698)	(7,338)	(7,445)	(7,333)
Program surplus (deficit)	69	(542)	(976)	(1,419)	(579)	98
Net interest charges	(1,051)	(1,056)	(928)	(925)	(714)	(795)
DBRS-Adjusted Surplus (Deficit)	**(982)**	**(1,597)**	**(1,904)**	**(2,344)**	**(1,293)**	**(697)**
Less: revenue risk adjustment	-	-	(125)	-	-	-
Add: adjustment for capital expenditures	205	517	199	137	287	308
Add: non-recurring revenues (expenditures)	-	-	-	-	-	-
Surplus (deficit), as reported	**(778)**	**(1,080)**	**(1,830)**	**(2,207)**	**(1,006)**	**(389)**
DBRS-Adjusted Debt Burden*	16,558	15,095	16,286	14,519	10,635	9,722
Gross provincial cash requirements	1,717	1,717	3,011	2,605	1,031	522
Gross capital expenditure	1,074	1,307	1,679	1,108	807	1,107

* Tax supported debt+municipal debt+unfunded pension liabilities

Selected Financial Indicators
(DBRS adjusted)

	Budget 2017-18	2016-17	Budget 2016-17	2015-16	2014-15	2013-14
Debt* as % of GDP	54.3%	50.4%	55.0%	48.2%	31.3%	28.2%
Surplus (deficit) as % of GDP	(3.2%)	(5.3%)	(6.4%)	(7.8%)	(3.8%)	(2.0%)
Net interest charges as % of revenue	14.4%	14.5%	13.8%	15.6%	10.4%	10.7%
Total tax revenue as % of revenue	53.4%	50.4%	54.3%	53.3%	44.1%	41.0%
Federal transfers as % of revenue	17.3%	16.8%	17.6%	17.9%	14.7%	13.7%
Resource revenues % of revenue	12.6%	14.0%	8.3%	9.9%	24.1%	30.8%
Total expenditure % of revenue	113.5%	122.0%	128.3%	139.6%	118.8%	109.4%
Health spending as % of total expenditures	38.2%	35.6%	35.1%	38.5%	37.1%	35.2%
Total revenue growth	0.2%	22.7%	13.6%	(13.8%)	(7.6%)	(0.3%)
Program expenditure growth	(7.6%)	6.4%	4.9%	(1.4%)	1.5%	1.3%
Total expenditure growth	(6.8%)	7.2%	4.4%	1.3%	0.4%	2.1%

* Tax-supported debt + municipal debt + unfunded pension liabilities

Political Background Information

Party in Power:	Liberal	30 of 40
Premier:	Dwight Ball	October 2019

Revenues ($ millions)	Budget 2017-18	Projected 2016-17	Budget 2016-17	2015-16	2014-15	2013-14
Personal income tax	1,626	1,603	1,524	1,309	1,310	1,222
Retail sales tax	1,238	1,105	1,171	905	937	907
Gasoline tax	274	317	328	193	186	186
Corporate income tax	378	261	259	350	219	358
Payroll tax	137	143	131	132	120	111
Tobacco tax	162	160	164	159	161	147
Other	73	71	73	105	98	114
Total Taxes	**3,887**	**3,661**	**3,650**	**3,153**	**3,030**	**3,045**
Mining and offshore royalties	919	1,019	555	585	1,658	2,286
Vehicle drivers' licences	96	95	89	84	72	74
Other fees and fines	387	383	383	227	243	206
Interest income	12	14	14	21	27	33
Liquor profits	173	174	177	163	161	155
Lottery revenues	138	137	142	155	124	128
Nalcor Energy	130	136	90	(19)	116	96
Other revenues	280	421	438	491	430	390
Total Own-Source Revenue	**6,022**	**6,040**	**5,537**	**4,859**	**5,860**	**6,412**
Equalization and offsets			-	-	-	-
Canada Health and Social Transfer	736	725	720	685	680	713
Other federal sources	520	498	464	374	326	307
Total Federal Government Transfers	**1,256**	**1,224**	**1,185**	**1,059**	**1,006**	**1,020**
Total DBRS-Adjusted Revenue	**7,278**	**7,264**	**6,722**	**5,918**	**6,866**	**7,432**
DBRS adjustment (sinking fund earnings)	61	56	54	54	55	56
Other non-recurring income	-	-	-	-	-	-
Total revenue, as reported	**7,339**	**7,320**	**6,776**	**5,973**	**6,921**	**7,487**

Expenditures	Budget 2017-18	Projected 2016-17	Budget 2016-17	2015-16	2014-15	2013-14
Health	3,157	3,151	3,026	3,178	3,025	2,861
Education	2,025	2,088	2,133	2,083	1,899	1,950
Child youth and family services	99	102	174	173	154	156
Resources and trade	261	262	291	337	390	300
Transportation and works	434	422	444	449	469	437
General government	335	645	805	351	638	765
Justice and public safety	249	257	258	271	256	240
Other	444	362	369	359	328	317
Net capital expenditures	205	517	199	137	287	308
DBRS-Adjusted Program Expenditures	**7,209**	**7,805**	**7,698**	**7,338**	**7,445**	**7,333**
Net interest charges 1	1,051	1,056	928	925	714	795
DBRS-Adjusted Expenditures	**8,261**	**8,861**	**8,626**	**8,262**	**8,159**	**8,129**
DBRS adjustment (sinking fund earnings)	61	56	54	54	55	56
Adjustments for capital expenditures 2	(205)	(517)	(199)	(137)	(287)	(308)
Total expenditures, as reported	**8,116**	**8,400**	**8,481**	**8,180**	**7,927**	**7,876**

1 Interest costs are net of sinking fund income.
2 DBRS recognizes capital expenditures as incurred (pay-as-you-go basis) rather than as amortized.

Province of Newfoundland and Labrador

Consolidated Balance Sheet

($ millions)	As at March 31				As at March 31		
Financial Assets	**2016**	**2015**	**2014**	**Liabilities**	**2016**	**2015**	**2014**
Cash and marketable securities	2,244	1,334	1,583	Treasury bills	2,092	778	493
Accounts receivable	485	555	920	Payables and accrued liab.	2,784	2,819	1,958
Loans and investments	355	395	336	Unfunded pens. liab.	2,055	1,783	3,908
Equity in gov't enterprises	3,592	2,818	2,426	Debt	9,485	7,285	4,626
Other	5	5	6	Employee benefits	2,771	2,609	2,554
Non-financial assets	4,484	4,349	4,148	Other liabilities	147	161	816
Total Financial Assets	11,164	9,456	9,419	**Total Liabilities**	**19,334**	**15,437**	**14,356**
				Accumulated Deficit	**(8,170)**	**(5,981)**	**(4,937)**

Public Sector Debt

($ millions)	2018B	2017P	2016	2015	2014	2013	2012	2011	2010
Direct debt 1	12,382	10,786	10,346	6,617	6,116	6,108	6,121	6,451	6,653
Promissory notes to fund pension contributions	2,171	2,203	2,603	2,636	-	-	-	-	-
Less: sinking funds	(1,589)	(1,492)	(1,361)	(1,268)	(1,272)	(1,198)	(1,085)	(1,083)	(994)
Net Direct Debt	**12,965**	**11,497**	**11,587**	**7,985**	**4,844**	**4,910**	**5,036**	**5,368**	**5,659**
Housing	87	92	97	103	110	116	122	130	135
Municipal	330	352	346	301	326	408	436	424	494
Other	337	378	434	503	534	539	491	633	616
Total other tax-supported debt	**753**	**822**	**877**	**907**	**970**	**1,062**	**1,049**	**1,187**	**1,245**
Total Tax-Supported Debt	**13,717**	**12,319**	**12,464**	**8,892**	**5,814**	**5,972**	**6,085**	**6,554**	**6,904**
Self-Supported Debt									
Nalcor Energy & Newfoundland and Labrador Hydro	6,635	6,300	6,300	6,225	1,225	1,225	1,225	1,225	1,225
Less: sinking funds	(417)	(405)	(398)	(508)	(497)	(482)	(467)	(443)	(427)
Net hydro debt 2	6,218	5,895	5,902	5,717	728	743	758	782	798
Total public sector debt	22,314	18,359	14,794	11,531	6,701	6,828	7,313	7,686	8,152
Unfunded Pension Liabilities 3	**2,840**	**2,776**	**2,055**	**1,743**	**3,908**	**3,270**	**3,090**	**2,667**	**2,177**
Total DBRS-Adjusted Debt	**16,558**	**15,095**	**14,519**	**10,635**	**9,722**	**9,242**	**9,174**	**9,221**	**9,081**
Per Capita ($)									
Tax-supported debt	26,014	23,238	23,576	16,831	11,023	11,344	11,589	12,557	13,361
Tax-supported debt + unfunded pension liab.	31,401	28,474	27,463	20,129	18,433	17,556	17,474	17,665	17,574
As a % of GDP									
Tax-supported debt	45.0%	41.1%	41.4%	26.1%	16.9%	18.6%	18.1%	22.5%	27.6%
Tax-supported debt & unf. pension liab.	54.3%	50.4%	48.2%	31.3%	28.2%	28.9%	27.4%	31.7%	36.3%
Direct Debt Breakdown by Currency 4									
CAD pay	94.6%	94.3%	92.6%	89.0%	83.6%	84.6%	84.8%	85.5%	85.5%
Non-CAD pay	5.4%	5.7%	7.4%	11.0%	16.4%	15.4%	15.2%	14.5%	14.5%

As at March 31

B = Budget P = Projected
1 Excludes $1.2 billion of pre-borrowing completed in 2016-17
2 Includes provincially guaranteed debt of NL Hydro and federally guaranteed debt of Muskrat Falls
3 Includes unamortized experience gains and losses
4 Including hedges (if any)

Direct Debt Breakdown by Interest Rate Type [4, 5]

	As at March 31								
	2018B	2017P	2016	2015	2014	2013	2012	2011	2010
Fixed rate	93.7%	93.5%	79.7%	81.4%	90.6%	91.4%	88.0%	88.4%	88.9%
Floating rate	6.3%	6.5%	20.3%	18.6%	9.4%	8.6%	12.0%	11.6%	11.1%

Gross Market Debt Maturity Profile [6]

As at March 31, 2017	2017-18	2018-19	2019-20	2020-21	2021-22	2023-27	2028+	Total
Direct provincial debt ($ millions)	780	237	235	942	466	3,481	5,500	11,641
- % of total	6.7%	2.0%	2.0%	8.1%	4.0%	29.9%	47.2%	100.0%

4 Including hedges (if any).
5 Floating rate debt is defined as debt that matures or is repriced within 12 months.
6 Does not include all debt.

Rating History

	Current	2016	2015	2014	2013	2012
Issuer Rating	A (low)	A (low)	A	A	A	A
Long-Term Debt	A (low)	A (low)	A	A	A	A
Short-Term Debt	R-1 (low)	R-1 (low)	R-1 (low)	R-1 (low)	R-1 (low)	R-1 (low)

Previous Action

- Confirmed, November 10, 2016.

Related Research

- *Rating Canadian Provincial Governments,* May 15, 2017.
- *DBRS Criteria: Guarantees and Other Forms of Support,* February 13, 2017.

Previous Report

- Newfoundland and Labrador, Province of: Rating Report, November 10, 2016.

Notes:
All figures are in Canadian dollars unless otherwise noted

For the definition of Issuer Rating, please refer to Rating Definitions under Rating Policy on www.dbrs.com.

Generally, Issuer Ratings apply to all senior unsecured obligations of an applicable issuer, except when an issuer has a significant or unique level of secured debt.

The DBRS group of companies consists of DBRS, Inc. (Delaware, U.S.)(NRSRO, DRO affiliate); DBRS Limited (Ontario, Canada)(DRO, NRSRO affiliate); DBRS Ratings Limited (England and Wales)(CRA, DRO affiliate); and DBRS Ratings México, Institución Calificadora de Valores S.A. de C.V. (Mexico)(CRA, NRSRO affiliate, DRO affiliate). Please note that DBRS Ratings Limited is not an NRSRO and ratings assigned by it are non-NRSRO ratings. For more information on regulatory registrations, recognitions and approvals, please see: http://www.dbrs.com/research/225752/highlights.pdf.

MOODY'S
INVESTORS SERVICE

CREDIT OPINION
27 July 2017

Update

Rate this Research

RATINGS

Newfoundland and Labrador, Province of

Domicile	Canada
Long Term Rating	Aa3
Type	Senior Unsecured - Fgn Curr
Outlook	Negative

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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Newfoundland and Labrador, Province of

Update to Discussion of Key Credit Factors

Summary Rating Rationale

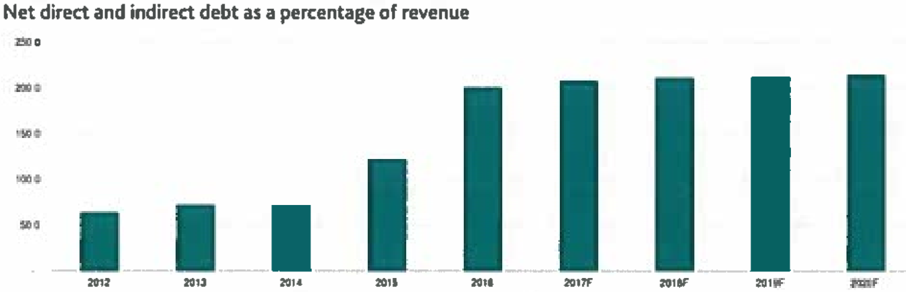
The Aa3 debt rating for the Province of Newfoundland and Labrador reflects 1) the fiscal flexibility to enact spending and revenue measures to align budgetary imbalances, 2) the presence of a comprehensive plan to align revenues with expenditures, 3) recent pension reforms which will produce long-term savings offset by 4) an expected deterioration of fiscal health stemming from a series of significant consolidated deficits due primarily to material decrease in offshore royalties, 5) a relatively narrow economic base focused on natural resource development and 6) growing contingent liability of the province's wholly owned energy company, Nalcor.

As a result of low revenues due to a decline in offshore royalties and weak economic outlook, Newfoundland and Labrador is expected to face several years of significant budgetary deficits. However, better than expected results for 2016/17, resulting from higher oil production, and a re-profiling of the timing of financing requirements may result in a faster stabilization of the province's debt burden than previously forecasted. However, the province continues to face elevated execution risk given the strong emphasis containing expenditure growth plays in the province's plan to return to balanced budgets. If deficit targets are not achieved, the province's debt burden would continue to rise across the medium-term.

Exhibit 1

Better than anticipated results in 2016/17 and a re-profiling of financing requirements suggest Newfoundland and Labrador's debt burden may stabilize over the medium-term

Net direct and indirect debt as a percentage of revenue



Source: Moody's Investors Service, Newfoundland and Labrador Financial Statements and 2017/18 Budget

National Peer Comparisons

The Province of Newfoundland and Labrador is rated at the low end of Canadian provinces, whose ratings span a narrow range from Aaa to Aa3. To finance a series of deficits, we forecast that the province's level of net direct and indirect debt relative to revenues is expected to rise to 215% by 2020/21. Along with a high debt burden, we also expect that Newfoundland and Labrador will sustain the highest interest expense relative to revenue (15%) of Canadian provinces through to 2023.

Credit Strengths

» Fiscal flexibility to align budgetary imbalance

» Comprehensive plan to cope with budgetary imbalances

» Decrease in unfunded pension liability and favourable maturity schedule partly mitigates increase in debt

Credit Challenges

» Prolonged period of deficits will weaken key fiscal metrics

» Relatively narrow economic base to remain weak over medium-term

» Growing contingent liability of Nalcor due to Muskrat Falls cost overruns

Rating Outlook

The rating outlook is negative, reflecting the potential for further fiscal pressure and higher debt burden and interest expense if the province fails to achieve its ambitious budget targets.

Factors that Could Lead to an Upgrade

» The outlook could be revised to stable if the province is able to execute its revenue and expenditure measures as planned and achieve the budget targets

» Evidence of debt accumulation stabilizing at lower than forecasted levels

Factors that Could Lead to a Downgrade

» Failure to achieve its budgetary targets, leading to higher and more persistent deficits than planned

» Higher than expected levels of interest or debt relative to revenue

Key Indicators

Exhibit 2
Newfoundland and Labrador, Province of

(Year Ending 3/31)	2015	2016	2017F	2018B	2019F
Net Direct and Indirect Debt as a % of Revenues	122.4	200.6	208.5	211.9	212.6
Net Direct and Indirect Debt as a % of GDP	24.9	39.8	51.5	51.3	53.5
Consolidated Surplus (Deficit) as a % of Revenues	(14.5)	(37.0)	(14.8)	(10.6)	(8.4)
Cash Financing Surplus (Requirement) as a % of Revenues	(4.2)	(32.8)	(44.8)	(23.6)	(11.0)
Total Interest Expense as a % of Revenues	6.0	13.7	15.2	15.2	14.6
Intergovernmental Transferes as a % of Revenue	14.5	17.7	16.7	17.1	16.5
Real GDP Growth (%) [1]	(2.0)	(0.7)	(3.8)	(0.2)	0.3

[1] Corresponds to calendar year.
Source: Moody's Investors Service, Provincial Financial Statements

Detailed Rating Considerations

The Province of Newfoundland and Labrador's Aa3 rating combines (1) a baseline credit assessment (BCA) for the province of a2 and (2) a high likelihood of extraordinary support coming from the Government of Canada (Aaa, stable) in the event that Newfoundland and Labrador faced acute liquidity stress.

Baseline Credit Assessment

FISCAL FLEXIBILITY TO ALIGN BUDGETARY IMBALANCE

The institutional framework governing relations, powers and responsibilities between Canadian provinces and the Federal government is well developed and stable. This framework provides Canadian provinces unfettered access to a broad range of tax bases and wide discretion over expenditure decisions, allowing provinces significant flexibility in its financial management. Compared to their counterparts in other countries, such as the German Länder and the Australian states, Canadian provinces enjoy far greater autonomy in terms of both the spending and revenue sides of their budgets. As such, Canadian provinces benefit from a high degree of fiscal policy flexibility that is more akin to that of sovereign governments than to many of their international sub-sovereign peers.

COMPREHENSIVE PLAN TO COPE WITH BUDGETARY IMBALANCES

Newfoundland and Labrador continues to face significant fiscal pressure from low levels of revenues stemming from the low oil price environment. To offset this revenue loss (relative to past years), the province continues to follow a multi-year budget plan that fully utilizes the fiscal flexibility inherent in Canadian provinces.

On the revenue side, the province introduced a wide range of tax measures in 2016, including increase to the provincial share of the Harmonized Sales Tax (HST), increases to income tax rates and the establishment of a temporary deficit reduction levy.

On the expenditure side, the province is balancing upward pressure arising from inflation and salary increases through efficiency efforts including zero based budgeting for departments, and changes to management structure. Across the entire period 2017/18-2022/23, program expenses are expected to fall 4.3%, with spending relatively flat across the last three years in particular.

The joint efforts on both revenue and expenses are expected to help return the province to balanced budgets by 2022/23 after having posted a consolidated deficit equal to 37% of revenue in 2015/16.

While we consider this multi-year plan to be ambitious, the province posts a per capita spending much higher than both the national average and average for the Maritime provinces, which would suggest that Newfoundland and Labrador has scope to find savings. Additionally, forecasted outcomes for the first year of the government's plan for was in line with budget levels.

DECREASE IN PENSION LIABILITY AND FAVOURABLE MATURITY SCHEDULE PARTLY MITIGATES ANTICIPATED INCREASE IN DEBT

A material portion of the expected rise in Newfoundland and Labrador's debt metrics includes the inclusion of promissory notes the province issued in return for pension reforms which will provide long-term savings for the province.

In 2014, the province issued a CAD2.685 billion promissory note, upon joint sponsorship of the Public Service Pension Plan (PSPP), which amortizes in equal quarterly payments amounting to CAD195 million annually over 30 years. Subsequently, the province also agreed to issue a CAD1.8 billion promissory note, upon joint sponsorship with the Teacher's Pension Plan, also amortizing over 30 years. These promissory notes are expected to account for nearly 30% of the province's net direct and indirect debt by the end of March 2017.

While unfunded pension liabilities are viewed as debt-like and are included in contingent liabilities, and therefore taken into the creditworthiness of a province, they are not specifically included in our metrics of net debt for Canadian provinces. As the province has converted a contingent liability to a formal obligation, this action is credit neutral despite having an impact on the province's debt burden. The province's addressing its unfunded pension liability and reduce the likelihood that it will worse, is credit positive.

The high debt burden is also mitigated by a favourable maturity schedule over the medium-term. We note that the province has very little debt maturing during the period 2016-2020, followed by a further favourable maturity schedule across 2021-2025. Furthermore, across the period 2026-2043 the province has several years with no debt maturing, allowing the province the flexibility to issue debt with various maturity dates while continuing to minimize annual debt repayments.

PROLONGED PERIOD OF DEFICITS WILL WEAKEN KEY FISCAL METRICS

Given the magnitude of the negative fiscal position the province faces, we anticipate a lengthy period before the province returns to balance. Despite the fiscal measures on both the revenue and expenditure side of their ledger, the province faces execution risk to achieve its plan to return to balanced budgets by 2022/23, including revenue risk stemming from oil price forecasts that exceed our own price range of $40-60 per barrel over the medium-term and ambitious expenditure constraint that will see expenditures decline slightly over the period 2018/19-2022/23, a rare example of true austerity within the Canadian provincial context.

After recording a forecasted deficit in 2015/16 equivalent to 37.0% of revenues, the province is expected to have recorded a noticeable improvement in 2016/17 (14.8%). However, annual improvements are expected to be smaller in future years, resulting in consolidated deficits between 10.6% in 2017/18 and 8.4% in 2018/19, levels that will apply materially negative pressure to the province's credit profile.

To fund the series of deficits, Newfoundland and Labrador's debt burden has already risen considerably, from 72.1% of revenue in 2013/14 to an expected 208.5% in 2016/17. Better than expected results for 2016/17 (forecasted deficit of CAD1.08 billion (14.8% of revenue) compared to the budgeted CAD1.83 billion deficit (27.0% of revenue)), owing largely to higher than expected oil production volumes, and a subsequent re-profiling of the timing of debt requirements has nonetheless shifted downward our base case assumption for the province's medium-term debt burden to 215% of revenue. Nonetheless, the province is still forecasting a 2017/18 deficit of CAD778 million (10.6%) which will weigh on financing requirements. The province's debt burden remains at risk of material increases greater than anticipated should the province fail to lower its deficit to a more manageable level (5% of revenue).

Given the higher debt burden, interest expense has also increased, reaching 15.2% in 2017/18. However, with lower than previously planned financing requirements, we now forecast that the interest burden will remain relatively stable, albeit at a high level, over the medium-term. The province nonetheless remains at greater risk than most other Canadian provinces of potential interest rate increases over the medium-term.

RELATIVELY NARROW ECONOMIC BASE TO REMAIN WEAK OVER MEDIUM-TERM

In part due to the higher costs of transporting goods to and from the province, as well as its small population, Newfoundland and Labrador has a relatively narrow economy with an important focus on natural resource development. Future development and expansion of economic activity is thus likely to remain muted as long as commodity price weakness persists. Depressed economic activity weakens the province's ability to raise revenue and therefore places risk on the province's plans for a return to balanced budgets.

The province forecasts that real GDP contracted in 2016 (-0.7%) and will contract again in 2017 (-3.8%) and 2018 (-0.2%), related primarily to the completion of large infrastructure and other construction projects currently underway. Capital investment is expected to decline across the next 4 years as little new investment is expected to begin to offset the lost economic activity related to the completion of current and recent projects. Nonetheless, the province's construction of a hydroelectric dam at Muskrat Falls and transmission line will continue to support important economic activity over the next few years, although this project is largely at peak construction currently and as such will diminish over the medium-term as the it moves closer to completion.

The provincial unemployment rate is expected to reach 17% in 2021. The high unemployment rate reflects both an expected deterioration in the labour market, but also the province's continued dependency on seasonal and rural industries. The duality between the wealthy oil-related sectors and the weaker traditional industries of the province represents a credit challenge and may pose complications in terms of the province's efforts to reduce spending as rural regions will likely continue to require higher per capita spending due to increased demands for social services. However, the relative improved wealth metrics across the province have allowed average personal incomes to surpass the national average and are well above levels seen in the other Atlantic provinces.

Despite the current low oil price forecasts, oil production and exploration activity is expected to remain an important component of the province's economy over the medium-term. New technology and updated retrievable reserve levels have provided extensions to the production life span of current oil fields. Continued interest in geological data surrounding the presence of potential sites for new exploration help to reassure that oil production will remain a significant share of the economy for the foreseeable future.

GROWING CONTINGENT LIABILITY OF NALCOR DUE TO MUSKRAT FALLS COST OVERRUNS

Nalcor, the province's wholly owned energy corporation, is in the midst of constructing a dam and hydroelectric generating station at Muskrat Falls, along the Churchill River in Labrador, as well as a transmission line from Labrador to the island of Newfoundland. Although the initial cost estimate was CAD6.2 billion, and received a CAD5 billion loan guarantee provided by the Federal government, Nalcor confirmed in June 2017 that construction costs have been revised to CAD10.1 billion.

While we view Nalcor as self-supporting, given its ability to generate sufficient revenues to ensure it does not rely on operating subsidies from the province, we nonetheless view its debt obligations as contingent liabilities of the province. While we do not anticipate to alter our view that Nalcor is self-supporting, should its financial position weaken, the possibility that it would require some support from the province will increase.

Further, although legislation has already been passed to ensure that hydro rates are set such that Nalcor will be able to service its debt, the rate increases necessary to cover the higher costs of the project could become sufficiently elevated. This may create pressure on the province to find offsetting measures, such as through reduced tax burdens or increased tax credits which will impact the provincial creditworthiness.

Extraordinary Support Considerations

Moody's assigns a high likelihood of extraordinary support from the Government of Canada (Aaa, stable), reflecting Moody's assessment of the incentive provided to the federal government of minimizing the risk of potential disruptions to capital markets if Newfoundland and Labrador, 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.

Output of the Baseline Credit Assessment Scorecard

In the case of Newfoundland and Labrador, the BCA scorecard (presented below) generates an estimated BCA of aa3, compared to the BCA of a2 assigned by the rating committee. The matrix-generated BCA 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 (Aaa, stable). The two notch differential reflects the backwards looking aspect of the scorecard which fails to capture the expected increase in debt relative to revenues, increase in interest expense and large persistent negative gross operating balances.

The idiosyncratic risk scorecard and BCA matrix, which generates estimated baseline credit assessments from a set of qualitative and quantitative credit metrics, are tools used by the rating committee in assessing regional and local government credit quality. The credit metrics captured by these tools provide a good statistical gauge of stand-alone credit strength and, in general, higher ratings can be expected among issuers with the highest scorecard-estimated BCAs. Nevertheless, the scorecard-estimated BCAs do not substitute for rating committee judgments regarding individual baseline credit assessments, nor is the scorecard a matrix for automatically assigning or changing these assessments. Scorecard results have limitations in that they are backward-looking, using historical data, while the assessments are forward-looking opinions of credit strength. Concomitantly, the limited number of variables included in these tools cannot fully capture the breadth and depth of our credit analysis.

Rating Methodology and Scorecard Factors

Exhibit 3

Newfoundland and Labrador, Province of

Baseline Credit Assessment	Score	Value	Sub-factor Weighting	Sub-factor Total	Factor Weighting	Total
Scorecard						
Factor 1: Economic Fundamentals						
Economic strength	3	109.13	70%	3.6	20%	0.72
Economic volatility	5		30%			
Factor 2: Institutional Framework						
Legislative background	1		50%	1	20%	0.20
Financial flexibility	1		50%			
Factor 3: Financial Performance and Debt Profile						
Gross operating balance / operating revenues (%)	9	-21.63	12.5%	5	30%	1.65
Interest payments / operating revenues (%)	9	10.26	12.5%			
Liquidity	1		25%			
Net direct and indirect debt / operating revenues (%)	9	200.60	25%			
Short-term direct debt / total direct debt (%)	3	19.10	25%			
Factor 4: Governance and Management - MAX						
Risk controls and financial management	5			5	30%	1.50
Investment and debt management	1					
Transparency and disclosure	5					
Idiosyncratic Risk Assessment						**4.07(4)**
Systemic Risk Assessment						**Aaa**
Suggested BCA						**aa3**

Source: Moody's Investors Service

Ratings

Exhibit 4

Category	Moody's Rating
NEWFOUNDLAND AND LABRADOR, PROVINCE OF	
Outlook	Negative
Senior Unsecured	Aa3

Source: Moody's Investors Service

S&P Global
Ratings

RatingsDirect®

Research Update:

Province of Newfoundland and Labrador Outlook Revised To Stable From Negative On Expected Improved Budgetary Results

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Research Update:

Province of Newfoundland and Labrador Outlook Revised To Stable From Negative On Expected Improved Budgetary Results

Overview

- We are revising our outlook on the Province of Newfoundland and Labrador to stable from negative.
- We are also affirming our 'A' long-term issuer credit and senior unsecured debt ratings as well as our 'A-1' short-term and commercial paper ratings on the province.
- The outlook revision reflects our expectations that, within the next two years, the government will continue to implement its fiscal response of revenue and expenditure measures, leading to improving budgetary results and a deceleration in the growth of direct and tax-supported debt burdens.

Rating Action

On July 14, 2017, S&P Global Ratings revised its outlook on the Province of Newfoundland and Labrador (Newfoundland) to stable from negative. At that time, S&P Global Ratings affirmed its 'A' long-term issuer credit and senior unsecured debt ratings as well as its 'A-1' short-term and commercial paper ratings on the province; and its 'A' issue-level rating on Newfoundland and Labrador Hydro's (NLH) provincially guaranteed senior unsecured debt.

Outlook

The stable outlook reflects our expectations that the government will continue to implement its fiscal response of revenue and expenditure measures, which will lead to improving budgetary results and a deceleration in the growth of its debt burden. We expect that, within the next two years, operating deficits will fall below 5% of operating revenues and after-capital deficits will decline to less than 10% of total revenues; and the province's tax-supported debt burden will remain below 180% of operating revenues. We also expect that cash and temporary investments will remain above or close to C$1 billion. Despite annual declines in real GDP in 2017 and 2018, GDP per capita should remain high.

Downside scenario

A reversal of government policy that threatens fiscal sustainability, leading to increasing operating and after-capital deficits and rising direct and tax-supported debt burdens; or a material drop in liquidity levels, such that cash and liquid assets represent less than 40% of prospective debt service could lead us to take a negative rating action.

Upside scenario

The return to operating balance and after-capital deficits falling to less than 10% of total revenues on a sustained basis, a material increase in cash and temporary investments, or a return to average growth prospects could result in a positive outlook or upgrade.

Rationale

The outlook revision reflects our view that the government's fiscal policy response first implemented early in fiscal 2017 (year ended March 31), which increased operating revenues and tightly contained expenditure growth, will lead to stabilized budgetary results and debt burden. We expect these fiscal improvements to take place against a backdrop of modest declines in real GDP in 2017 and 2018 as oil prices remain close to US$50 per barrel. We expect that the government would take further fiscal measures to mitigate revenue shortfalls that might arise if oil prices are lower than the prices assumed in the budget.

Budgetary performances will continue to strengthen in fiscal 2018 as debt burden growth decelerates.

The improvement in Newfoundland's budgetary results, seen in fiscal 2017, should continue in fiscal 2018 and 2019. The province's after-capital deficits should improve to 10% of total revenues in fiscal 2018 and less than 9% by fiscal 2020. Newfoundland's after-capital deficit was more than 30% of total revenues in fiscal 2016. We expect the operating deficit to weaken slightly in fiscal 2018 to about 7.6% of operating revenues, before declining to about 3% by fiscal 2020. The improvement expected in budgetary performance is the result of the government's fiscal policy response to the plunge in oil prices that began in 2014. The policy response, which the government implemented beginning in fiscal 2017, includes tax and fee increases and a number of measures to contain or reduce spending. The spending plan has already yielded savings and we expect that those savings will increase annually in the next two fiscal years. Under our base-case forecast for fiscal years 2016-2020, we expect that Newfoundland will record an average operating deficit of under 10% of operating revenues and average after-capital deficits of about 16% of total revenues. We continue to believe that oil price volatility means considerable volatility in the province's budgetary results, which tempers our assessment of its budgetary performances.

The rapid growth in the debt burden should decelerate with strengthening budgetary results. Newfoundland's debt burden, however, will continue to be high compared with that of peers over our two-year outlook horizon. Tax-supported debt, which includes direct debt net of sinking funds and the guaranteed debt of NLH (about C$1.2 billion, or about 16% of operating revenues), should be about C$12.7 billion, or 163% of operating revenues, by fiscal year-end 2017; and rise further to about C$14.9 billion, or 174%, by fiscal year-end 2020. The province tax-supported debt stood at 94% of operating revenues at fiscal year-end 2015. Under our base-case scenario, we expect that the province's interest expense burden will average 8% operating revenues in the fiscal 2017-2019 period. We believe that Newfoundland's unfunded pension and other postemployment benefit liabilities, which we estimate will represent more than 100% of operating revenues in fiscal 2017, weigh on the province's credit profile.

We expect that Newfoundland will have cash and temporary investments of close to C$1.1 billion by the end of fiscal 2018, which is down from about C$2.3 billion at fiscal year-end 2017. We believe these will remain close to or above C$1 billion through to the end of fiscal 2020. We estimate that the province's free cash and liquid assets represent almost 70% of its upcoming debt service obligations (including all maturities) in the next 12 months. These measures exclude Newfoundland's sinking fund, which exceeded C$1.3 billion as of the end of fiscal 2017. Instead, we net the province's sinking fund from its tax-supported debt burden in our analysis. Our assessment of Newfoundland's liquidity also reflects our view that the province has strong access to Canada's well-developed capital markets, although volatility in liquidity ratios offsets this, in our opinion.

The government's determination in implementing its fiscal response, increasing taxes substantially and beginning a multiyear expenditure reduction initiative that will likely be unpopular at times, bolsters our assessment of Newfoundland's budgetary flexibility. We expect that modifiable revenues will average 83% of operating revenues for the 2016-2020 fiscal period. Capital spending in absolute terms will be fairly stable in this fiscal year and the next two, averaging about 6.6% of total spending for the 2016-2020 fiscal period.

The province's primary contingent risk relates to the operating risk of its wholly owned local energy provider, Nalcor Energy, a holding company that owns NLH. Nalcor (through two trusts) has issued close to C$8 billion of bonds that it used to finance the Muskrat Falls hydroelectric project and its associated transmission lines. That debt was issued through a special-purpose vehicle and carries a guarantee from the Government of Canada. We believe the province has a strong incentive to provide extraordinary government support to Nalcor in the event of financial stress. This view primarily stems from the essential nature of NLH's service responsibilities, as well as the political and economic importance of Nalcor's other development projects like Muskrat Falls.

Newfoundland's recession will continue through 2017 and 2018 but GDP per capita will remain high.

We believe that Newfoundland's GDP per capita will continue to easily exceed US$38,000 through the base-case forecast period. Real GDP growth, however, will remain negative in 2017 and 2018 (negative 3.8% and negative 0.2%, respectively). We believe positive GDP growth will not return until 2019. The province has been in recession since 2014. Nominal GDP growth rates, on the other hand, will be positive in 2017 and 2018 at 1.8% and 3.2%, respectively.

We expect that GDP per capita should reach close to C$58,000 by the end of 2017. Labor force results have been unfavorable due to the recession; employment has been falling and will continue to do so in the next two years. The unemployment rate should reach 13.9% in 2017, rising again in 2018 and 2019. Both the economy's significant exposure to the oil industry and its low growth prospects, which are a direct result of the fall in oil prices, temper our assessment of Newfoundland's economy.

We view the province's financial management favorably. The ruling Liberal Party has a large majority in the legislature, and is not constrained in its ability to pass the revenue and expenditure measures needed to restore fiscal balances. The government has already acted decisively, in our opinion, in implementing its two-pronged fiscal policy response, through the tax increases and expenditure reductions. Because of the volatility of oil prices, variances in the revenue budget can be significant. Budget assumptions are generally what we consider conservative. We believe debt management and related policies are prudent and risk averse.

Newfoundland benefits from Canada's provincial-federal institutional framework. The province receives significant transfers from the federal government through Canada Health Transfer and Canada Social Transfer payments. Total transfers (operating and capital) will represent under C$1.3 billion in fiscal 2018, or about 17% of operating revenues.

Key Statistics

Table 1

Province of Newfoundland and Labrador -- Selected Indicators

	--Fiscal year ended March 31--					
(Mil. C$)	**2014**	**2015**	**2016**	**2017bc**	**2018bc**	**2019bc**
Operating revenues	6,760	5,940	7,231	6,991	7,453	7,732
Operating expenditures	7,083	7,452	7,597	7,521	8,025	7,968
Operating balance	(323)	(1,512)	(366)	(530)	(572)	(236)
Operating balance (% of operating revenues)	(4.8)	(25.5)	(5.1)	(7.6)	(7.7)	(3.1)
Capital revenues	56	33	89	273	108	89
Capital expenditures	556	428	785	479	503	524
Balance after capital accounts	(823)	(1,908)	(1,061)	(736)	(967)	(671)
Balance after capital accounts (% of total revenues)	(12.1)	(31.9)	(14.5)	(10.1)	(12.8)	(8.6)
Debt repaid	1,257	33	1,386	150	235	200
Gross borrowings	1,298	3,725	2,925	875	1,600	975
Balance after borrowings	(782)	1,785	478	(11)	398	104
Modifiable revenues (% of operating revenues)	85.1	83.3	83.1	82.0	82.2	83.6
Capital expenditures (% of total expenditures)	7.3	5.4	9.4	6.0	5.9	6.2

Table 1

Province of Newfoundland and Labrador -- Selected Indicators (cont.)						
	--Fiscal year ended March 31--					
(Mil. C$)	2014	2015	2016	2017bc	2018bc	2019bc
Direct debt (outstanding at year-end)	5,349	8,984	10,494	10,793	12,158	12,933
Direct debt (% of operating revenues)	79.1	151.3	145.1	154.4	163.1	167.3
Tax-supported debt (outstanding at year-end)	6,876	10,422	12,153	12,733	14,098	14,873
Tax-supported debt (% of consolidated operating revenues)	93.6	154.4	150.9	162.9	170.3	173.8
Interest (% of operating revenues)	5.7	7.1	6.2	8.8	8.9	9.3
Local GDP per capita (C$)	63,345	56,932	56,531	57,848	59,973	63,024
National GDP per capita (C$)	55,792	55,405	55,876	57,800	59,340	60,780

Note: 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. Base case reflects S&P Global Ratings' expectations of the most likely scenario. Downside case represents some but not all aspects of S&P Global Ratings' scenarios that could be consistent with a downgrade. Upside case represents some but not all aspects of S&P Global Ratings' scenarios that could be consistent with an upgrade. bc--Base case.

Ratings Score Snapshot

Table 2

Province of Newfoundland and Labrador -- Ratings Score Snapshot	
Key rating factors	**Assessment**
Institutional Framework	Very predictable and well-balanced
Economy	Average
Financial Management	Strong
Budgetary Flexibility	Very strong
Budgetary Performance	Very weak
Liquidity	Less than adequate
Debt Burden	Very high
Contingent Liabilities	High

Note: S&P Global Ratings' credit ratings on local and regional governments are based on eight main rating factors listed in the table above. Section A of S&P Global Ratings' "Methodology For Rating Non-U.S. Local And Regional Governments," published on June 30, 2014, summarizes how the eight factors are combined to derive the foreign currency rating on the government.

Key Sovereign Statistics

Sovereign Risk Indicators, July 6, 2017. Interactive version available at http://www/spratings.com/sri

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017

- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria - Governments - International Public Finance: Methodology For Rating Non-U.S. Local And Regional Governments, June 30, 2014
- Criteria - Governments - International Public Finance: Methodology And Assumptions For Analyzing The Liquidity Of Non-U.S. Local And Regional Governments And Related Entities And For Rating Their Commercial Paper Programs, Oct. 15, 2009
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Newfoundland and Labrador (Province of)		
Issuer credit rating	A/Stable/A-1	A/Negative/A-1

Ratings Affirmed

Newfoundland and Labrador (Province of)	
Senior unsecured	AA/Stable
Senior unsecured	A
Commercial paper	
Global scale	A-1
Canada scale	A-1(Mid)
Newfoundland and Labrador Hydro	
Senior unsecured	A
Commercial paper	
Global scale	A-1
Canada scale	A-1(Mid)

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.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.