

Research Update:

Regional Municipality of York Ratings Raised To 'AAA' From 'AA+' On Improved Debt Assessment

July 29, 2021

Overview

- We are raising the issuer credit and senior unsecured debt ratings on the Regional Municipality of York to 'AAA' from 'AA+'. The upgrade reflects York's exceptionally strong finances, steady debt levels, and falling interest burden, which the region has maintained despite the COVID-19 pandemic.
- We believe York's diverse economy and relatively wealthy residents provide strong support for regional revenues, while management has demonstrated prudence and flexibility to appropriately limit spending.
- We expect that York will continue to proceed carefully with its capital spending program, making changes where appropriate, and continue to limit its debt issuance to levels below the peak in 2017.
- The stable outlook reflects our view of the stability of regional revenues, and York's commitment to maintain strong public finances.

PRIMARY CREDIT ANALYST

Jennifer Love, CFA
Toronto
+ 1 (416) 507 3285
jennifer.love
@spglobal.com

SECONDARY CONTACT

Adam J Gillespie
Toronto
+ 1 (416) 507 2565
adam.gillespie
@spglobal.com

Rating Action

On July 29, 2021, S&P Global Ratings raised its long-term issuer credit and senior unsecured debt ratings on the Regional Municipality of York to 'AAA' from 'AA+'.

Outlook

The stable outlook reflects our expectation that, in the next two years, a recovering economy will continue to support development in the region, fueling strong budgetary surpluses; and that a high level of growth-related capital revenues will support the capital program. We expect this will help maintain after-capital surpluses and mitigate the need for external financing such that York's tax-supported debt burden will remain below 120% of consolidated operating revenues through 2023, and that its interest burden will remain below 5% of consolidated operating revenues. Furthermore, we expect the region will carefully monitor growth and development charge collections to ensure capital spending remains consistent with population growth.

Downside scenario

We could lower the ratings if York generated lower-than-expected revenue, resulting in much weaker operating balances and sustained, material after-capital deficits of more than 10% of total revenues. We could also lower the ratings if a similar scenario resulted in lower operating balances, and rising debt that led to an interest burden above 5% of revenues.

Rationale

The upgrade reflects York's exceptionally strong finances, steady debt levels, and falling interest burden, which the region has maintained despite the pandemic. In 2020, the region continued to generate strong revenues, primarily via its stable property tax base, which makes up almost 50% of revenues. The region also prudently imposed cost-mitigation strategies and benefited from federal and provincial funding in 2020. York ultimately posted a C\$944 million adjusted operating surplus and an after-capital surplus of C\$364 million, reducing the need for external funding. The region continues to limit new debt issuance to fund growth-related spending and maintain net debt below its 2017 peak. The region's interest costs have fallen below 5% of consolidated operating revenues and we expect York's interest burden will remain below 5% during the outlook horizon. York's liquidity remains exceptional. The ratings also reflect the region's strong financial management, which we believe will continue to adapt the capital plan and related expenses to align with fluctuations in population growth.

Strong revenue generation and related budgetary surpluses support creditworthiness, while we expect the debt burden will remain stable in the next two years.

York's revenues remained strong in 2020, despite the pandemic, and the region employed cost-mitigation strategies to further support budgetary balances, leading to very high operating and after capital balances. We expect the region will continue generating strong and stable operating balances averaging almost 31% of operating revenues in our base-case scenario for 2019-2023. Furthermore, these surpluses should support York's capital plans and result in after-capital surpluses of about 13% of total revenues, on average, during the same period. Historically, the region's rising population and assessment values have supported York's revenues, while also putting pressure on growth-related capital spending. In recent years, the region implemented strategies around capital asset replacement and more flexible delivery of growth-related infrastructure, which have resulted in large asset replacement reserves and lower debt issuance. The region has also allocated some of its surpluses to capital reserves to minimize related debt issuance. We view York as having high budgetary flexibility, owing to its above-average household incomes and relatively low tax rates, which we think would support additional regional revenue generation, if necessary.

We expect annual surpluses and strong reserves will continue to fund the region's capital plan and reduce York's reliance on debt funding. We expect capital spending will average about C\$650 million per year through 2024, with spending focused on roads, transit, and, to a lesser degree, water and wastewater. The current 10-year capital plan allocates C\$7.8 billion to capital projects, of which 30% will be debt-financed. Management expects reserves will contribute the bulk of capital funding. We expect York's debt burden (net of sinking funds) will remain stable at 94% of consolidated operating revenue in 2022. Over the past few years, York's interest burden has fallen

and now averages 4.3% of operating revenues. In addition, the region's debt burden now represents less than five years of operating surpluses, which further mitigates our assessment of the debt burden.

York demonstrates exceptional liquidity, with liquidity balances that significantly exceed debt servicing requirements. We believe that cash and investment balances (excluding long-term net sinking funds and deferred revenue) will total almost C\$3.2 billion in the next 12 months, sufficient to cover more than 1,202% of the total debt service forecast. We believe York's access to external liquidity is strong, in part because of its frequent issuance and its practice of maintaining benchmark issues that bolster liquidity for its debt in the secondary markets. Although the region's capital expenditure plans could cause near-term liquidity to fluctuate, we expect ongoing efforts to build capital reserves will support the liquidity position in the next two years.

A diverse economy supports York's revenues; very strong management and institutional framework also boosts the region's creditworthiness.

Our very strong economic assessment reflects our belief that York's diverse and wealthy economy will continue to support GDP per capita above the national average and growth in line with that of Canada. York's economy benefits from its proximity to and integration with the City of Toronto. The region boasts the sixth-largest municipal population in Canada, with an estimated 1.2 million residents in 2020, as well as a sizable employment base of 599,700 jobs. Recent population growth has been manageable, in the 1%-2% range annually. Building activity and assessment growth have generally been robust and will continue to support revenue increases. Furthermore, York's well-diversified economy should continue to support revenue growth throughout the business cycle, in our view. Assessment growth has averaged about 1.7% annually over the past five years.

We believe York's financial management is very strong and in line with that of regional peers. York's long-term capital plan has evolved in the past several years, reflecting both revised growth estimates and greater financial discipline, and we believe management demonstrates the flexibility to appropriately align capital plans with fluctuations in population growth. The region produces a multiyear budget that matches the term of council and from which management develops annual budgets with achievable revenue and expenditure targets. Moreover, the region has an established commitment to fiscal sustainability through its fiscal strategy process, which successive regional councils have endorsed.

We believe York, similar to other Canadian municipalities, benefits from a very predictable and well-balanced local and regional government framework that has demonstrated a high degree of institutional stability. Although provincial governments mandate a significant proportion of municipal spending, they also provide operating fund transfers and impose fiscal restraint through legislative requirements to pass balanced operating budgets. Municipalities generally have the ability to match expenditures well with revenues, except for capital spending, which can be intensive. Any operating surpluses typically fund capital expenditures and future liabilities (such as postemployment obligations and landfill closure costs) through reserve contributions.

Key Statistics

Table 1

Regional Municipality of York--Selected Indicators

(Mil. C\$)	--Year ended Dec. 31--					
	2018	2019	2020	2021bc	2022bc	2023bc
Operating revenues	2,381	2,537	2,614	2,694	2,701	2,816
Operating expenditures	1,892	1,837	1,670	1,840	1,900	1,998
Operating balance	489	700	944	854	801	818
Operating balance (% of operating revenues)	20.5	27.6	36.1	31.7	29.6	29.1
Capital revenues	306	170	88	259	298	267
Capital expenditures	344	637	668	607	697	702
Balance after capital accounts	451	233	364	506	401	383
Balance after capital accounts (% of total revenues)	16.8	8.6	13.5	17.2	13.4	12.4
Debt repaid	161	162	177	206	210	219
Gross borrowings	40	349	410	125	195	237
Balance after borrowings	329	420	596	425	386	401
Direct debt (outstanding at year-end)	2,898	2,833	2,904	2,799	2,746	2,660
Direct debt (% of operating revenues)	121.7	111.7	111.1	103.9	101.7	94.5
Tax-supported debt (outstanding at year-end)	2,898	2,833	2,904	2,799	2,746	2,660
Tax-supported debt (% of consolidated operating revenues)	121.7	111.7	111.1	103.9	101.7	94.5
Interest (% of operating revenues)	5.6	5.0	4.7	4.2	4.1	4.2
Local GDP per capita (single units)	N/A	N/A	N/A	N/A	N/A	N/A
National GDP per capita (single units)	60,196	61,466	58,016	65,195	67,992	69,683

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. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. N/A--Not applicable. N.A.--Not available. N.M.--Not meaningful.

Ratings Score Snapshot

Table 2

Regional Municipality of York--Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	1
Financial management	1
Budgetary performance	1
Liquidity	1
Debt burden	2

Table 2

Regional Municipality of York--Ratings Score Snapshot (cont.)

Key rating factors	Scores
Stand-alone credit profile	aaa
Issuer credit rating	AAA

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

Sovereign Risk Indicators, July 12, 2021. An interactive version is available at <http://spratingscom.sri>.

Related Criteria

- Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Economic Outlook Canada Q3 2021: Growth Setback In The Spring Will Give Way To Summer Boom, June 25, 2021
- S&P Global Ratings Definitions, Jan. 5, 2021
- Public Finance System: Canadian Municipalities, May 12, 2020
- Guidance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 2019
- Institutional Framework Assessments For International Local And Regional Governments, June 4, 2021

Ratings List

Upgraded

	To	From
York (Regional Municipality of)		
Senior Unsecured	AAA	AA+

Upgraded; Outlook Action

	To	From
York (Regional Municipality of)		
Issuer Credit Rating	AAA/Stable/--	AA+/Positive/--

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

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