

Research Update:

County of Simcoe 'AA' Issuer Credit Rating Affirmed; Outlook Remains Stable

November 6, 2019

Overview

- The County of Simcoe benefits from a healthy budgetary performance with high operating balances, very low debt levels, and robust liquidity.
- We are affirming our 'AA' long-term issuer credit rating and maintaining our stable outlook on the county.

Rating Action

On Nov. 6, 2019, S&P Global Ratings affirmed its 'AA' long-term issuer credit rating on the County of Simcoe, in the Province of Ontario. The outlook is stable.

Outlook

The stable outlook reflects our expectation that Simcoe will increase its capital spending in 2019, resulting in an after-capital deficit of 3% of total revenues, but that it will post near-balanced results in 2020 and 2021 as capital needs ease. We estimate tax-supported debt will decrease to a very low 7% of operating revenues in 2021 as most of the projects will be internally financed. We believe available liquidity will cover all debt service costs in the next two years. Following the conclusion of the province's regional government review, we do not expect to see a material impact to the county's budget, debt, or liquidity metrics.

Downside scenario

In the next two years, we could take a negative rating action if greater-than-expected capital spending increased after-capital deficits past 5% of total revenues and increased debt levels past 60% of operating revenues.

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Upside scenario

We could take a positive rating action in the next two years if more detailed medium-term financial planning coupled with modest economic momentum that strengthens budgetary performance leads to consistent after-capital surpluses.

Rationale

We have updated our base-case scenario for Simcoe and extended our forecast horizon through 2021. We estimate Simcoe will continue generating healthy operating surpluses and that it will post an after-capital deficit of 3% of total revenues in 2019 as a result of large capital requirements before returning to a near-balanced position in 2020 and 2021 as capital needs ease. We expect Simcoe will keep managing its capital program prudently, with a strong reliance on pay-as-you-go financing, and avoid the need to issue large amounts of debt in the next two years. We also expect that the county will continue to benefit from prudent financial management practices and a robust liquidity position.

Financial management is prudent and institutions remain broadly supportive but a less favorable socioeconomic profile is a rating constraint.

Simcoe benefits from an advantageous location, along the Highway 400 transportation corridor and close to the Greater Toronto Area. It also benefits from a sizable public sector, including local schools and hospitals, as well as the Canadian Forces Base Borden, which helps stabilize the local economy. While GDP per capita is not available at the local level, we believe that it would be in line with the national level of US\$46,400 based on Simcoe's income levels. In our opinion, slower population growth and weaker demographic trends relative to those of peers in the Greater Toronto Area result in a less favorable socioeconomic profile that could negatively affect the labor pool and hinder investment in the county. However, Simcoe's focus on diversifying its economy as well as attracting and retaining young and skilled workers could start reversing these trends.

Management demonstrates political and managerial strength through generally good political consensus in passing budgets and a good degree of transparency and disclosure in its financial statements. It also prepares detailed operating and capital budgets with prudent spending practices. However, capital spending is typically lower than the annual budget. We believe the county demonstrates relevant expertise through adequate planning and monitoring although the accuracy of the long-term financial plan tends to decrease as the time horizon increases. The county has a robust set of financial policies. While we consider the debt policy prudent, Simcoe lacks a formal liquidity policy.

We believe Canadian municipalities benefit from a very predictable and well-balanced institutional 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.

Healthy operating balances will help the capital plan remain manageable and will allow Simcoe to keep very low debt and robust liquidity.

In our base-case scenario for 2017-2021, we expect operating balances to remain high at 11% of operating revenues on average. We estimate capital projects related to affordable housing projects and paramedic services will increase capital spending in 2019, resulting in an after-capital deficit of 3% of total revenues. Nevertheless, we expect capital needs will ease in the next two years, resulting in a near-balanced position on average in 2017-2021.

Simcoe's current financial plan considers that it will continue to fund its capital projects with internal resources in the next three years. Therefore, we estimate that tax-supported debt will slowly decrease to about 7% of operating revenues in 2021, from about 10% in 2018. Although there is a possibility that Simcoe could decide to issue debt to fund some projects in 2020 and 2021, including a runway expansion at Lake Simcoe Regional Airport, we believe that the debt burden would remain less than 30% of operating revenues. The county's tax-supported debt represents less than five years of operating surpluses, which mitigates the debt burden, in our opinion. Interest costs accounted for 1% of operating revenues in 2018 and we expect they will remain stable during our two-year outlook horizon.

In our opinion, Simcoe's liquidity remains strong. We estimate total free cash in the next 12 months of about C\$70 million will be enough to cover more than 22x the estimated debt service for the period. We expect this ratio will remain well above 100% during the outlook horizon. Similar to that of its domestic peers, the county's access to external liquidity is satisfactory.

Key Statistics

Table 1

County of Simcoe -- Selected Indicators

(Mil. C\$)	--Fiscal year-end Dec. 31--					
	2016	2017	2018	2019bc	2020bc	2021bc
Operating revenues	308	328	371	384	387	396
Operating expenditures	275	305	321	336	345	357
Operating balance	33	23	50	47	43	39
Operating balance (% of operating revenues)	10.7	7.0	13.5	12.3	11.0	9.9
Capital revenues	34	44	33	60	45	43
Capital expenditures	71	53	84	120	90	87
Balance after capital accounts	(4)	14	(2)	(12)	(2)	(4)
Balance after capital accounts (% of total revenues)	(1.2)	3.9	(0.5)	(2.8)	(0.5)	(1.0)
Debt repaid	11	3	3	3	3	1
Gross borrowings	0	0	0	0	0	0
Balance after borrowings	(16)	12	(4)	(15)	(5)	(6)
Direct debt (outstanding at year-end)	41	38	36	33	30	29
Direct debt (% of operating revenues)	13.2	11.7	9.6	8.7	7.9	7.3

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Table 1

County of Simcoe -- Selected Indicators (cont.)

(Mil. C\$)	--Fiscal year-end Dec. 31--					
	2016	2017	2018	2019bc	2020bc	2021bc
Tax-supported debt (outstanding at year-end)	41	38	36	33	30	29
Tax-supported debt (% of consolidated operating revenues)	13.2	11.7	9.6	8.7	7.9	7.3
Interest (% of operating revenues)	0.4	0.3	0.3	0.1	0.1	0.1
Local GDP per capita (single units)	N/A	N/A	N/A	N/A	N/A	N/A
National GDP per capita (single units)	56,169	58,607	59,879	61,413	63,082	65,120

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. dc--Downside case represents some but not all aspects of S&P Global Ratings' scenarios that could be consistent with a downgrade. uc--Upside case represents some but not all aspects of S&P Global Ratings' scenarios that could be consistent with an upgrade. N/A--Not applicable.

Ratings Score Snapshot

Table 2

County of Simcoe -- Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	2
Economy	2
Financial management	3
Budgetary performance	2
Liquidity	1
Debt burden	1
Stand-alone credit profile	aa
Issuer credit rating	AA

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, Oct. 10, 2019, 2019. Interactive version available at <http://www.spratings.com/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: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- For Canada, Below-Potential Growth Is Likely In The Near Term, Oct. 7, 2019
- Credit Conditions North America: Rising Recession Risk Adds To Trade, Rate Uncertainty, Sept. 30, 2019
- 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, July 4, 2019
- Public Finance System Overview: Canadian Municipalities, July 18, 2018

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

Ratings Affirmed

Simcoe (County of)

Issuer Credit Rating AA/Stable/--

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

Research Update: County of Simcoe 'AA' Issuer Credit Rating Affirmed; Outlook Remains Stable

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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