S&P Global Ratings

RatingsDirect®

Research Update:

Regional Municipality of York 'AAA' Issuer Credit Rating Affirmed; Outlook Remains Stable

July 9, 2024

PRIMARY CREDIT ANALYST

Hector Cedano, CFA

Toronto

+ 1 (416) 507 2536

hector.cedano@spglobal.com

SECONDARY CONTACT

Jennifer Love, CFA

Toronto

+ 1 (416) 507 3285

jennifer.love@spglobal.com

Overview

- The Regional Municipality of York benefits from solid budgetary performance with high operating balances and manageable capital expenditures. It also benefits from very ample liquidity.
- We affirmed our 'AAA' long-term issuer credit and senior unsecured debt ratings on York.
- The stable outlook reflects our expectation that the region will post lower, but positive, balances after capital accounts as it proceeds with its capital plan. It also reflects our expectation of a continued decline in York's debt burden.

Rating Action

On July 9, 2024, S&P Global Ratings affirmed its 'AAA' long-term issuer credit and senior unsecured debt ratings on the Regional Municipality of York, in the Canadian Province of Ontario. The outlook remains stable.

Outlook

The stable outlook reflects S&P Global Ratings' expectation that York will maintain strong operating surpluses in the next two years and that its balances after capital accounts will fall but remain positive as it proceeds with its capital plan. In addition, we expect that its debt burden will continue to decline.

Downside scenario

Although unlikely, we could lower the ratings in the next two years if York generated lower-than-expected revenue and we believed its flexibility to raise revenue was constrained. If this resulted in weaker operating performance, sustained after-capital deficits of more than 5% of total revenue, and a weaker-than-expected debt burden, we could take a negative rating action.

Rationale

We expect that York's diverse and wealthy economy will continue to foster economic stability. The region, in our view, will keep posting healthy operating balances, and its balances after capital accounts will fall but remain positive as it proceeds with its capital plan.

York will issue debt to help fund part of its capital spending plan, but we expect a continued decline in its debt burden as a result of debt repayment, contributions to sinking funds, and revenue growth. We estimate that debt service coverage will remain well above 100% in our forecast horizon.

A strong economy and prudent financial management will remain key to the region's creditworthiness

We expect that the region's economic strengths will continue to foster fiscal stability and support the ratings. 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 1.26 million residents in 2023, as well as a sizable employment base of about 610,000 jobs. The region's economy has added more than 30,000 jobs since 2019 with very important contributions from the finance, insurance, and real estate sectors. Building activity and assessment growth continue to support regional revenue.

Municipal GDP data is unavailable, but we believe York's GDP per capita is higher than Canada's, based on the region's high income levels. Our estimate for Canada's GDP per capita in 2024 is about US$53,800.

We believe York's financial management is very strong and in line with that of its regional peers. York's long-term capital plan has evolved in recent years, reflecting both revised growth estimates and greater financial discipline, and we believe management demonstrates the flexibility to appropriately align the region's capital plan with fluctuations in population growth. The region produces a multiyear budget that matches the term of the York Regional Council; from that multiyear budget, 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. The council continues to endorse the building of several reserves and is proactively raising funds for a subway extension via a dedicated levy.

As do other Canadian municipalities, York benefits from an extremely predictable and supportive local and regional government framework that has demonstrated high institutional stability and provided systemic extraordinary support in times of financial distress. Most recently through the pandemic, senior levels of government provided operating and transit-related grants to municipalities, in addition to direct support to individuals and businesses.

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 revenue, except for capital spending, which can be intensive. Any operating surpluses typically fund capital expenditures and future liabilities (such as postemployment obligations) through reserve contributions.

Municipalities have demonstrated a track record of strong budget results. As such, debt burdens, on average, are low relative to those of global peers, and growth over time has been modest.

Budgetary performance will remain strong, and the debt burden will continue to decline

Our expectation is that York's operating balances will remain strong--at 27% of operating revenue, on average, in 2022-2025. These surpluses should support York's capital plan, which includes an eight-kilometer extension of the Yonge Street subway line north to Richmond Hill. The region budgeted C$1.12 billion starting in 2022 to fund its share of the project; it plans to partially fund the project via a dedicated levy. Another important project in the capital plan is a project to enlarge and improve the York Durham Sewage System, which will require new water and wastewater servicing infrastructure.

We believe after-capital surpluses will decline as York proceeds with its capital plan; we see after-capital surpluses at 13% of total revenue, on average, in 2022-2026. York has high budgetary flexibility, in our view, owing to its above-average household incomes and relatively low tax rates. We think they would support additional revenue generation, if necessary.

Historically, the region's rising population and assessment values have supported revenue while also putting pressure on growth-related capital spending. We see these pressures abating somewhat, with population growth moderating to 1%-2% per year. Furthermore, in recent years, the region implemented strategies for capital asset replacement and more flexible delivery of growth-related infrastructure, which have resulted in the accumulation of large asset replacement reserves and lower debt issuance.

Our expectation is that operating surpluses, dedicated funding, and strong reserves will continue to fund York's capital plan and reduce its reliance on debt funding. The region continues to limit new debt issuance to fund growth-related spending, and it's still keeping net debt below its 2017 peak. In addition, we estimate that it will receive higher development charges, which will lessen the need for debt issuance. As a result, we expect that York will issue about C$266 million of debt in 2024-2026, less than what we estimated in our previous base case.

Even as it issues new debt, we expect that York's debt burden (net of sinking funds) will continue to decrease--to 53% of operating revenue in 2026 from 77% in 2023--as a result of debt repayment, contributions to sinking funds, and revenue growth. In addition, the region's direct debt represents less than five years of operating surpluses, which mitigates our assessment of the debt burden. Interest costs accounted for about 3.5% of operating revenue in 2023, and we expect those costs to stay below 5% of operating revenue during the two-year outlook horizon.

York has exceptional liquidity, in our view. We estimate that total free cash in the next 12 months will be enough to cover more than 16x the estimated debt service for the period. We expect that this ratio will remain well above 100% during the outlook horizon.

In addition, we believe York's access to external liquidity is strong, in part because of its frequent issuances and its practice of maintaining benchmark issues that bolster liquidity for its debt in the secondary markets.

Key Statistics

Table 1

Regional Municipality of York--Selected indicators

(Mil. C$)	2021	2022	2023	2024bc	2025bc	2026bc
Operating revenue	2,664	2,795	3,063	3,164	3,264	3,363
Operating expenditures	1,878	1,990	2,249	2,328	2,400	2,468
Operating balance	786	805	815	836	864	894
Operating balance (% of operating revenue)	29.5	28.8	26.6	26.4	26.5	26.6
Capital revenue	209	220	289	297	405	437
Capital expenditures	506	518	553	672	918	991
Balance after capital accounts	489	506	551	460	351	341
Balance after capital accounts (% of total revenue)	17.0	16.8	16.4	13.3	9.6	9.0
Debt repaid	206	214	215	231	235	239
Gross borrowings	300	0	105	35	138	93
Balance after borrowings	582	292	440	265	254	195
Direct debt outstanding at year-end	2,711	2,472	2,362	2,185	2,022	1,790
Direct debt (% of operating revenue)	101.8	88.5	77.1	69.0	61.9	53.2
Tax-supported debt outstanding at year-end	2,711	2,472	2,362	2,185	2,022	1,790
Tax-supported debt (% of consolidated operating revenue)	101.8	88.5	77.1	69.0	61.9	53.2
Interest (% of operating revenue)	4.3	3.9	3.5	3.7	3.7	3.5
Local GDP per capita (single units)	N/A	N/A	N/A	N/A	N/A	N/A
National GDP per capita (single units)	65,825	72,249	72,047	73,083	74,672	77,095

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.

Ratings Score Snapshot

Table 2

Regional Municipality of York--Rating component scores

Key rating factors	Scores
Institutional framework	1
Economy	1
Financial management	1
Budgetary performance	1
Liquidity	1
Debt burden	1
Stand-alone credit profile	aaa

Table 2

Regional Municipality of York--Rating component scores (cont.)

Key rating factors	Scores
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 "Methodology For Rating Local And Regional Governments Outside Of The U.S.," published 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 the 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, April 8, 2024. An interactive version is available at spratings.com/sri

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- 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 Research: Economic Outlook Canada Q3 2024: Turning The Corner, June 24, 2024
- Institutional Framework Assessment: Canadian Municipalities Employ Flexibilities Within Fiscal Framework To Temper Cost Pressures, April 2, 2024
- Sector And Industry Variables | Criteria | Governments | Sovereigns: Sovereign Rating Methodology, March 26, 2024
- S&P Global Ratings Definitions, June 9, 2023

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	
York (Regional Municipality of)	
Issuer Credit Rating	AAA/Stable/--
York (Regional Municipality of)	
Senior Unsecured	AAA

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.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.