S&P Global
Ratings

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Research Update:

City of Greater Sudbury 'AA' Ratings Affirmed; Outlook Stable

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Overview

- We expect the City of Greater Sudbury will continue demonstrating prudent financial management, allowing it to keep generating healthy operating surpluses, despite pandemic-related operating pressures.
- The city's elevated capital plan will widen after-capital deficits through 2022 and the debt-financing of some large, one-time projects will also increase the debt burden in the medium term.
- We are affirming our 'AA' long-term issuer credit and senior unsecured debt ratings on the city.
- The stable outlook reflects our expectation that the city will continue to generate healthy operating surpluses in the next two years and that its debt burden, although increasing, will remain manageable.

Rating Action

On Sept. 22, 2020, S&P Global Ratings affirmed its 'AA' long-term issuer credit and senior unsecured debt ratings on the City of Greater Sudbury, in the Province of Ontario. The outlook is stable.

Outlook

The stable outlook reflects our expectation that the city will continue to generate healthy operating surpluses, although after-capital deficits will widen materially in the next two years. Even though the pandemic is having near-term impacts on the local economy, we believe that the economy will recover gradually in the next two years and that the tax-supported debt burden will remain modest.

Downside scenario

We could lower the rating in the next two years if Sudbury's financial management practices significantly deteriorated, and we came to believe that sustained after-capital deficits greater than 10% of total revenues would persist beyond our current outlook horizon. In addition, continued economic deterioration or a lack of material recovery in the medium term could stress the ratings.

Upside scenario

We could raise the ratings if Sudbury manages to complete its extensive capital plan and return to after-capital balances that are in line with historical levels, and the debt burden declines to less than 30% of operating revenues. Alternatively, stronger-than-anticipated economic growth that led to a materially broader economic base could also result in a positive rating action.

Rationale

The slowdown in economic activity brought on by the COVID-19 pandemic and its associated restrictions will create a challenging operating environment for Sudbury in the next two years. We believe that the gradual diversification of the local economy, along with a healthy public sector, will aid the city in its recovery and help to mitigate the high exposure to the mining sector and associated price volatility. Furthermore, we expect that the city's cost-containment efforts will help to sustain robust operating balances, although large capital expenditures will push higher after-capital deficits and a higher debt burden throughout the forecast horizon.

Large capital spending will weigh on Sudbury's budgetary performance and increase the debt burden in the next two years.

Sudbury has projected that the pandemic will have a net financial impact on its operations of about C$6.2 million in 2020. Revenue losses stem mainly from lower collection of user fees (largely transit and recreation), while additional spending has been largely dedicated to public health measures. To counter this loss, the city implemented a number of cost-saving measures, such as salary gapping, freezing student hiring, and temporary layoffs. Subsequently, the city announced that it will receive C$12.7 million in funding from the federal Safe Restart program, which will offset the net impact in 2020 and provide some funding to mitigate revenue and expense impacts that are likely to drag into 2021. Despite the short-term challenges, we believe that the city will maintain healthy operating surpluses of more than 12% of operating revenues on average in 2018-2022. These surpluses have enabled Sudbury to internally finance the majority of its capital plan; however, we expect its capital spending will ramp up in the next several years, primarily to help address the infrastructure requirement, and complete several large projects, including an arena, an art gallery/library, and a new conference center. Consequently, we believe that after-capital deficits will rise significantly in the next two years and average almost 7% of total revenue in our 2018-2022 base case.

In March 2020, Sudbury issued C$200 million of bonds to finance several large, one-time projects, including an arena and event center. Based on the current borrowing plan, we expect that tax-supported debt will rise to about C$290 million in 2021, from C$61 million at the end of 2019. This will result in a significant increase in the city's debt burden, with a near-term peak of about 49% of operating revenue by the end of 2021, up from 11% in 2019. However, because this represents less than five years of operating surpluses, based on our forecast, we believe that the city will maintain significant capacity to manage the higher debt burden. In addition, we expect that interest costs will remain very manageable at 1% of operating revenues on average in 2019-2021. We do not believe that the liabilities of Sudbury's related entities, Sudbury Airport Community Development Corp. and Greater Sudbury Utilities Inc., represents a material contingent liability risk, as we believe the likelihood of the city providing extraordinary support to them in a stress scenario is low.

Sudbury's credit profile is bolstered by what we view as a very robust liquidity position and satisfactory access to external liquidity to meet financing needs. We estimate that the city will maintain about C$275 million of free cash in the next 12 months, sufficient to cover more than 19x the estimated debt service requirements.

A sizable public-sector presence partially mitigates exposure to volatile industries while strong financial management practices bolster the rating.

We believe Sudbury's economy will contract in 2020 and begin to recover over the next two years as social distancing measures ease. Despite what we view as a temporary shock, we believe Sudbury still demonstrates characteristics of a strong economy, with high median incomes and estimated GDP per capita about in line with that of the national economy at about US$42,000 in 2019. Historically a world leader in nickel mining, Sudbury has diversified its economy in the past 30 years and expanded from its resource-based economy to emerge as the major retail, economic, health, and educational center for northeastern Ontario. The public sector (health care, school boards, higher education, and municipal and provincial administration) is a stabilizing force, in our view, and has become an important contributor to the local economy. Nevertheless, employment remains fairly concentrated in the resource sector, primarily nickel mining, which accounts for about 20% of total local employment. We believe that the regional economy's relatively high reliance on the mining sector, and in particular its exposure to the volatility of nickel prices, could affect Sudbury's revenue growth and expenditure needs in the future, and partly constrains our assessment of the economic profile.

In our view, Sudbury's financial management practices are strong, and largely in line with those of similarly rated peers. The city provides transparent, easy-to-access disclosure of pertinent information and prepares robust operating and capital budgets. Its annual operating budget and five-year capital plan, which we view as realistic, reflect the broad goals outlined in the 10-year financial plan. Similar to its Canadian peers, Sudbury can only issue debt to finance capital expenditures, and we believe it has prudent and conservative policies as well as a stable and well-qualified management team to govern its debt and liquidity management.

We believe Sudbury, like other Canadian municipalities, benefits from a very predictable and well-balanced local 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. Operating surpluses typically fund capital expenditures and future liabilities (such as postemployment obligations and landfill closure costs) through reserve contributions.

Key Statistics

Table 1

City of Greater Sudbury -- Selected Indicators

	--Fiscal year-end Dec. 31--				
(Mil. C$)	2018	2019bc	2020bc	2021bc	2022bc
Operating revenues	541	560	579	592	612
Operating expenditures	468	492	509	522	535
Operating balance	72	68	71	70	76
Operating balance (% of operating revenues)	13.4	12.1	12.2	11.8	12.5
Capital revenues	33	41	56	70	74
Capital expenditures	105	104	194	199	255
Balance after capital accounts	0	5	(67)	(60)	(104)
Balance after capital accounts (% of total revenues)	0.0	0.9	(10.6)	(9.0)	(15.2)
Debt repaid	5	4	5	9	10
Gross borrowings	6	0	200	43	0
Balance after borrowings	1	1	128	(26)	(115)
Direct debt (outstanding at year-end)	66	61	256	290	280
Direct debt (% of operating revenues)	12.1	10.9	44.2	49.0	45.8
Tax-supported debt (outstanding at year-end)	66	61	256	290	280
Tax-supported debt (% of consolidated operating revenues)	12.1	10.9	44.2	49.0	45.8
Interest (% of operating revenues)	0.5	0.5	1.1	1.4	1.3
National GDP per capita (single units)	60,011	61,291	57,181	60,677	63,026

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

City of Greater Sudbury -- Ratings Score Snapshot

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

Table 2

City of Greater Sudbury -- Ratings Score Snapshot (cont.)

Key rating factors	Scores
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, July 14, 2020. An interactive version is 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

Related Research

- S&P Global Ratings Definitions, Aug. 7, 2020
- Canada's Economy Faces A Patchy Recovery, June 29, 2020
- 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, July 4, 2019

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	
Greater Sudbury (City of)	
Issuer Credit Rating	AA/Stable/--
Senior Unsecured	AA