

Research Update:

County of Wellington Ratings Affirmed At 'AAA'; Outlook Stable

September 19, 2022

Overview

- The County of Wellington's strong local economy supports healthy budgetary results, such that balances after capital accounts remain in a surplus during the two-year outlook horizon.
- Reliance on debt remains in line with expectations, keeping the burden, including on-lent debt, close to 30% of consolidated operating revenues.
- Accordingly, S&P Global Ratings affirmed its 'AAA' long-term issuer credit and senior unsecured debt ratings on the County of Wellington.
- The stable outlook reflects our view that a positive economic trajectory and prudent management will support strong financial results, with positive after-capital balances in the next two years. We also expect the county's execution of the capital plan will not result in a significantly higher reliance on debt or internal resources relative to our current expectations.

Rating Action

On Sept. 19, 2022, S&P Global Ratings affirmed its 'AAA' long-term issuer credit and senior unsecured debt ratings on the County of Wellington, in the Province of Ontario. The outlook is stable.

Outlook

The stable outlook reflects our expectation that Wellington will maintain healthy budgetary results, albeit modestly weaker during the two-year outlook horizon, with after-capital surpluses of about 1.5% of adjusted total revenues. We also expect that the county will continue to use debt as a source of capital funding such that its tax-supported debt will approach 30% of operating revenues. The county's liquidity position remains a credit strength.

Downside scenario

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Although unlikely, we could take a negative rating action in the next two years if, coupled with prolonged operating pressures, a larger-than-expected capital plan resulted in sustained after-capital deficits of more than 5% of total revenues. We would also expect management to increase reliance on debt such that the tax-supported debt burden rose to more than 60% of operating revenues.

Rationale

We expect Wellington's healthy and stable economy, with an increasing and relatively wealthy population, will support its revenues during the outlook horizon. Despite inflationary pressures on the cost of goods and personnel, which we expect will weaken near-term operating balances modestly, we project these will remain strong at more than 10% of operating revenues. We also expect management will remain prudent, with a focus on long-term fiscal sustainability, and will keep annual capital outlays and reliance on debt funding manageable. As a result, we project after-capital results to remain in a surplus and the increase in the debt burden to be modest, reaching 30% of consolidated operating revenues by 2024. The county's robust liquidity position is a key credit strength.

Economic fundamentals remain strong, despite ongoing global economic risks; institutions are supportive

Amid headwinds, we expect economic activity in Wellington will remain healthy and the county will continue to benefit from population increases. Wellington has a largely stable economy and an advantageous location, close to the Greater Toronto Area and the cities of Hamilton and Guelph, and along the Highway 401 corridor. Although municipal GDP data are unavailable, we believe that GDP per capita would be largely in line with the national level of more than US\$55,000, based on high income levels. In line with many domestic peers, and exacerbated by the pandemic, labor availability is a challenge. The county continues to work with the local municipalities and employers to help attract and retain workers.

Wellington's council and staff demonstrate stable, experienced, and effective leadership, and the county has prudent financial policies and practices that ensure a good degree of transparency and fiscal discipline. The county produces 10-year operating budgets and tax-rate projections, approved annually; and uses realistic underlying assumptions, in our view. It also produces a 10-year capital budget with corresponding funding sources.

As do other Canadian municipalities, Wellington benefits from an extremely predictable and supportive local and regional government framework that has demonstrated high institutional stability and evidence of 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 revenues, 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 and, therefore, debt burdens, on average, are low relative to those of global peers and growth over time has been modest.

Stable tax base supports projected after-capital surpluses, while increase in debt is manageable

We expect Wellington will maintain strong operating results in the next two years, albeit modestly weaker due to inflationary pressures and waning emergency pandemic support from senior levels of government. A strong underlying economy and growing population will support property tax collections, the largest component of revenues, keeping operating balances at more than 13% of operating revenues, on average, in 2020-2024. Similarly, although we expect after-capital results will moderate during the outlook horizon, these will remain in a surplus position, on average, in the five-year period. Although provincially mandated services and collective agreements with employees constrain Wellington's ability to cut spending somewhat, this is in line with other Canadian municipalities.

A track record of healthy operating results and accumulated reserves reduce Wellington's reliance on debt funding for capital. Capital grants from senior levels of government are also an important source of funding, allowing for increased investment in infrastructure improvements targeting road networks, bridges, and culverts. Roadwork accounts for almost 70% of the county's five-year capital plan. We expect Wellington's capital spending in the next two years will be largely in line with that in recent years at about C\$35 million annually.

We expect Wellington's tax-supported debt burden (including debt issued on behalf of lower-tier municipalities) will approach 30% of consolidated operating revenues in 2024. A large portion of future issuance is at the lower-tier level, and net of that, the county's own-purpose tax-supported debt will remain stable in the next two years, at about 15% of consolidated operating revenues. The county's debt profile also benefits from very modest interest costs of less than 1% of operating revenues. Exposure to contingent liabilities is limited, in our view.

Wellington maintains a robust liquidity position. We estimate free cash balances and investments will be about C\$170 million in the next 12 months, sufficient to cover more than 20x of projected debt service in the next 12 months. Similar to that of other Canadian municipalities, Wellington's access to external liquidity is satisfactory, in our view.

Key Statistics

Table 1

County of Wellington -- Selected Indicators

	--Fiscal year-end Dec. 31--					
	2019	2020	2021	2022bc	2023bc	2024bc
Operating revenues	200	213	226	227	226	231
Operating expenditures	178	177	195	195	199	205
Operating balance	23	36	31	32	27	26
Operating balance (% of operating revenues)	11.3	17.0	13.9	14.1	11.8	11.2
Capital revenues	15	9	15	13	13	13
Capital expenditures	34	33	22	30	35	35
Balance after capital accounts	4	13	25	15	5	4

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Table 1

County of Wellington -- Selected Indicators (cont.)

	--Fiscal year-end Dec. 31--					
	2019	2020	2021	2022bc	2023bc	2024bc
Balance after capital accounts (% of total revenues)	1.9	5.7	10.3	6.2	1.9	1.5
Debt repaid	7	9	6	6	7	6
Gross borrowings	10	0	7	7	6	19
Balance after borrowings	10	9	28	18	4	3
Direct debt (outstanding at year-end)	63	54	55	57	56	69
Direct debt (% of operating revenues)	31.5	25.5	24.5	25.1	24.9	29.8
Tax-supported debt (outstanding at year-end)	63	54	55	57	56	69
Tax-supported debt (% of consolidated operating revenues)	31.5	25.5	24.5	25.1	24.9	29.8
Interest (% of operating revenues)	1.1	1.0	0.8	0.8	0.8	0.7
National GDP per capita (single units)	61,469	58,016	65,186	69,471	70,786	71,954

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.

Ratings Score Snapshot

Table 2

County of Wellington -- Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	1
Economy	1
Financial management	2
Budgetary performance	1
Liquidity	1
Debt burden	1
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 11, 2022. An interactive version is available at <http://www.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

- Institutional Framework Assessments For International Local And Regional Governments, July 26, 2022
- Economic Outlook Canada Q3 2022: Near-Term Growth To Slow Amid Faster Rate Hikes And Surging Inflation, June 27, 2022
- Institutional Framework Assessment: Canadian Municipalities, June 1, 2022
- S&P Global Ratings Definitions, Nov. 10, 2021
- Guidance: Methodology For Rating Local And Regional Governments Outside Of The U.S., July 15, 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		
Wellington (County of)		
Issuer Credit Rating	AAA/Stable/--	
Wellington (County of)		
Senior Unsecured	AAA	

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