

**Credit Opinion: York, Regional Municipality of**

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Canada

**Ratings**

Category	Moody's Rating
Outlook	Stable
Bonds -Dom Curr	Aaa

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**Key Indicators**

York, Regional Municipality of (Year Ending 12/31)	2006	2007	[1]2008	2009	2010
Net Direct and Indirect Debt/Total Revenue (%)	92.8	88.4	69.8	95.4	91.3
Gross Operating Balance/Operating Revenue (%)	9.2	12.1	3.8	13.9	18.3
Cash Financing Surplus (Requirement)/Total Revenue (%)	(9.0)	6.3	5.8	(8.0)	(5.1)
Interest Payments/Operating Revenue (%)	4.0	4.5	4.1	5.0	5.0
Debt Service/Total Revenue (%)	9.4	10.1	9.1	11.2	9.7
Capital Spending/Total Expenditures (%)	30.8	29.8	23.5	49.1	64.8
Self-financing Ratio	0.7	1.2	1.3	0.8	0.9

[1] Accounting changes were introduced in 2009; 2009 and restated 2008 figures are not directly comparable to prior years. Accounting changes in 2009 include the adoption of PSAB section 3150 Tangible Capital Assets and changes in the presentation of financial statements, including the elimination of fund accounting.

**Opinion**

**SUMMARY RATING RATIONALE**

The Regional Municipality of York's Aaa debt rating reflects high reserve levels, prudent and far-sighted fiscal management and positive operating outcomes. While York's net direct and indirect debt, measuring 91.3% of total revenues at December 31, 2010, is expected to increase in the medium term, the municipality's reserves, which represented 89.8% of net direct and indirect debt at December 31, 2010, provide considerable liquidity and a measure of safety for debenture holders, supporting the Aaa rating. The rating also takes into consideration the region's diversified and growing economy and increased capital expenditure requiring additional debt.

## National Peer Comparisons

The Regional Municipality of York is rated at the high end of Canadian municipalities, whose ratings remain in a narrow range of Aaa-Aa2. The region's position relative to national peers reflects its high reserve levels and positive operating results. The institutional framework governing municipalities in Ontario is mature and well-developed, similar to that of other Canadian provinces where Moody's rates municipalities.

### **Credit Strengths**

Credit strengths for the Regional Municipality of York include:

- High levels of cash and investments
- Consistent, positive operating results
- Rapidly growing population and assessment base
- Mature, supportive framework governing municipalities in Ontario

### **Credit Challenges**

Credit challenges for the Regional Municipality of York include:

- Regional growth pressures leading to significant capital financing needs and increased debt issuance

### **Rating Outlook**

The outlook for York's Aaa rating is stable.

### **What Could Change the Rating - Down**

Given the fiscal discipline displayed by the local administration, it is unlikely that conditions could deteriorate by a large enough margin, in the near term, to trigger a downgrade. Nevertheless, a sustained loss of discipline, leading to increases in debt issuance beyond current expectations, combined with a decrease in the region's liquidity level, would apply downward pressure on the rating.

## **DETAILED RATING CONSIDERATIONS**

The rating assigned to York reflects the application of Moody's JDA rating methodology for regional and local governments. In accordance with this methodology, Moody's first establishes the baseline credit assessment (BCA) for York and then considers the likelihood of support from the Province of Ontario (Aa1, stable outlook) to avoid an imminent default by York, should this extreme situation ever occur.

### **Baseline Credit Assessment**

The Regional Municipality of York's BCA of 1 (on a scale of 1 to 21, in which 1 represents the lowest level of credit risk) reflects the following factors:

#### Financial Position and Performance

In recent years, the Regional Municipality of York has grown rapidly as it expands its services to meet demands from a rising population. Guided by a series of long-term strategic plans and an effective annual budget process that involves multi-year operating outlooks and 10-year capital expenditure projections, York has generally generated positive operating outcomes and overall surpluses, and growth in operating revenues has generally exceeded growth in operating expenditures.

In 2010, total revenues increased by 12.9%, driven by higher taxation revenues, user fees, and government

grants related to both operating and capital expenditures. own-source property tax revenue accounted for approximately 55.6% of operating revenues, while provincial operating grants and user fees represented 17.9% and 19.1% respectively. On the expenditure side, total expenses increased by 3.1%, as higher spending on areas such as protection to persons and property and transportation services were partially offset by lower expenses related to general government operations. Overall, the surplus for 2010 was equivalent to 27.4% of total revenues. Excluding

amortization expenses and revenues related to capital expenditures and development charges, the region's gross operating balance was equivalent to 18.3% of operating revenues, compared to 13.8% in 2009.

#### Debt Profile

While net debt as a percentage of total revenues decreased in 2010 due to strong revenue growth, in recent years, the implementation of capital plans to address growth pressures has led to a significant increase in York's debt burden. In 2010, York's net direct and indirect debt measured C\$1.6 billion, or 91.3% of total revenues, compared to C\$0.8 billion in 2005, or 75.1% of total revenues. Total debt service—which includes principal and interest payments—as a percentage of total revenues decreased slightly to 9.7% in 2010 from 11.2% in 2009 but has remained fairly stable in recent years.

York's latest 10-year capital plan (2011-2020) was approved by Regional Council in March 2011 and projects a total of C\$8.0 billion in capital expenditures. The 2011-2020 capital plan calls for C\$1.4 billion in capital expenditures in support of rapid transit, C\$2.2 billion for sewer infrastructure, C\$1.3 billion for roads and C\$1.5 billion for water infrastructure. While the capital plan calls for C\$3.9 billion in debt-financing, we expect that actual debt issuance will be lower than forecast. Even though the capital plan is front-end loaded—with 64.2% of capital spending and 63.5% of debt financing forecast over the next five years—the region typically underspends

its capital budget. Based on York's historical capital realization rates, we expect that under the current capital plan, the region's ratio of net direct and indirect debt to total revenues will increase to about 100% by 2014. Although York's debt is considered high relative to similarly rated Canadian municipalities, the region's rating is supported by its strong liquidity position. At the end of 2010, the combined balance in reserves, reserve funds and the development charges account was about C\$1.4 billion, equivalent to approximately 89.8% of net direct and indirect debt.

#### Governance and Management Factors

Similar to other highly rated municipalities in Ontario, York displays strong governance and management characteristics. In addition to long-term planning for capital and operating budgets and a history of meeting fiscal targets, management adheres to conservative debt and investment management policies, thus limiting the region's exposure to market-related risks and ensuring relatively smooth debt servicing costs. These fiscal management measures are also supported by comprehensive, transparent and timely fiscal reporting.

#### Economic Fundamentals

The Regional Municipality of York is located in the Greater Toronto Area (GTA) and benefits from its proximity to Canada's largest commercial and financial centre and adjacent U.S. markets. York's population continues to experience strong growth, increasing at an average rate of 3.8% between 1995 and 2010, reaching 1,061,983 in 2010 and representing about 17.1% of the GTA's population. York's population is also younger and more affluent than the Ontario average, which supports the regional tax base.

Employment in the region is well diversified across a variety of industries, including business services, retail and wholesale trade as well as finance and insurance. While the manufacturing sector remains the largest employer in the region, its share of employment decreased over the past ten years to 16.2% in 2010, from 23.6% in 1998, consistent with trends observed across Canada. The regional economy is nevertheless highly diverse and in June 2011, the unemployment rate in York was 7.6%, below the GTA average of about

8.6%.

## Operating Environment

The national operating environment in which York operates is typical of advanced industrial economies, characterized by high GDP per capita, low GDP volatility, and high ranking on the World Bank's Government Effectiveness Index, all of which suggest a minimal level of systemic economic, financial and political risk. As evidenced by Canada's record of continued economic expansion and political stability, the macroeconomic environment is robust and federal government institutions are responsive. Accordingly, the conditions that have historically preceded national crises associated with widespread defaults of regional and local governments are not present in Canada.

## Institutional Framework

The institutional framework governing municipalities in Ontario is mature and highly developed. The division of roles and responsibilities between the province and municipalities is clearly articulated. Historically, changes to the institutional framework have occurred at a measured, evolutionary pace, following discussions between both parties. Nevertheless, in certain cases, changes have occurred more rapidly.

York's creditworthiness benefits from the stability inherent in the provincial institutional framework. Provincial legislation dictates a high degree of oversight, including limits on debt servicing costs, while policy flexibility, on both the revenue and expenditure sides of the ledger, helps York to manage pressures as they arise.

## Extraordinary Support Considerations

York's Aaa rating is composed of a BCA of 1 and a very high likelihood that the Province of Ontario (rated Aa1, stable outlook) would act to prevent a default by York. The very high likelihood of support reflects Moody's assessment of the risk to Ontario's reputation as a regulator of municipalities and the incentive for the provincial government to minimize the risk of potential disruptions to capital markets if York, or any municipality, were to default.

Moody's rating committee also assigns a moderate default dependence level, reflecting the regional municipality and the province's joint exposure to common economic shocks.

## Output of the Baseline Credit Assessment Scorecard

In the case of York, the BCA scorecard (presented below) generates an estimated BCA of 2, roughly in-line with the BCA of 1 assigned by the rating committee.

The BCA scorecard, which generates estimated baseline credit assessments from a set of qualitative and quantitative credit metrics, is a tool used by the rating committee in assessing regional and local government credit quality. The credit metrics captured by the scorecard provide a good statistical gauge of stand-alone credit strength and, in general, higher ratings can be expected among issuers with the highest scorecard-estimated BCAs. Nevertheless, the scorecard-estimated BCAs do not substitute for rating committee judgments regarding individual baseline credit assessments, nor is the scorecard a matrix for automatically assigning or changing these assessments. Scorecard results have limitations in that they are backward-looking, using historical data, while the assessments are forward-looking opinions of credit strength. Concomitantly, the limited number of variables included in the scorecard cannot fully capture the breadth and depth of our credit analysis.

## ABOUT MOODY'S SUB-SOVEREIGN RATINGS

### National and Global Scale Ratings

Moody's National Scale Ratings (NSRs) are intended as relative measures of creditworthiness among debt issues and issuers within a country, enabling market participants to better differentiate relative risks. NSRs

differ from Moody's global scale ratings in that they are not globally comparable with the full universe of Moody's rated entities, but only with NSRs for other rated debt issues and issuers within the same country. NSRs are designated by a ".nn" country modifier signifying the relevant country, as in ".mx" for Mexico. For further information on Moody's approach to national scale ratings, please refer to Moody's Rating Implementation Guidance published in August 2010 entitled "Mapping Moody's National Scale Ratings to Global Scale Ratings."

The Moody's Global Scale rating for issuers and issues allows investors to compare the issuer's/issue's creditworthiness to all others in the world, rather than merely in one country. It incorporates all risks relating to that country, including the potential volatility of the national economy.

#### Country Ceilings for Foreign Currency Obligations

Moody's assigns a ceiling for foreign-currency bonds and notes to every country (or separate monetary area) in which there are rated obligors. The ceiling generally indicates the highest rating that can be assigned to a foreign-currency denominated security issued by an entity subject to the monetary sovereignty of that country or area. In most cases, the ceiling will be equivalent to the rating that is (or would be) assigned to foreign-currency denominated bonds of the government. Ratings that pierce the country ceiling may be permitted, however, for foreign-currency denominated securities benefiting from special characteristics that are judged to give them a lower risk of default than is indicated by the ceiling. Such characteristics may be intrinsic to the issuer and/or related to Moody's view regarding the government's likely policy actions during a foreign currency crisis.

#### Baseline Credit Assessment

Moody's baseline credit assessment incorporates the government's intrinsic credit strength and accounts for ongoing operating subsidies and transfers from the supporting government. In effect, the baseline credit assessment reflects the likelihood that a local government would require extraordinary support.

#### Extraordinary Support

Extraordinary support is defined as action taken by a supporting government to prevent a default by a regional or local government (RLG) and could take different forms, ranging from a formal guarantee to direct cash infusions to facilitating negotiations with lenders to enhance access to needed financing. Extraordinary support is described as either low (0% - 30%), moderate (31% - 50%), high (51% - 70%), very high (71% - 95%) or fully supported (96% - 100%).

#### Default Dependence

Default dependence reflects the likelihood that the credit profiles of two obligors may be imperfectly correlated. Such imperfect correlation, if present, has important diversifying effects which can change the joint-default outcome. Intuitively, if two obligors' default risks are imperfectly correlated, the risk that they would simultaneously default is smaller than the risk of either defaulting on its own.

In the application of joint-default analysis to RLGs, default dependence reflects the tendency of the RLG and the supporting government to be jointly susceptible to adverse circumstances leading to defaults. Since the capacity of the higher-tier government to provide extraordinary support and prevent a default by an RLG is conditional on the solvency of both entities, the more highly dependent -- or correlated -- the two obligors' baseline default risks, the lower the benefits achieved from joint support. In most cases, the close economic links and/or overlapping tax bases and/or close intergovernmental fiscal arrangements between different levels of government result in a moderate to very high degree of default dependence.

Default dependence is described as either low (0% - 30%), moderate (31% - 50%), high (51% - 70%) or very high (71% - 100%).

## Rating Factors

### York, Regional Municipality of

Baseline Credit Assessment			Sub-Factor	Sub-Factor	Factor	Total
Scorecard - 2010	Value	Score	Weighting	Total	Weighting	
<b>Factor 1: Operating Environment</b>						
National GDP per capita (PPP basis, \$US)	38,813	1	50.0%	1.50	50.0%	0.75
National GDP Volatility (%)	2.9	3	25.0%			
National Govt Effectiveness Index (World Bank)	1.87	1	25.0%			
<b>Factor 2: Institutional Framework</b>						
Predictability, Stability, Responsiveness	1	1	50.0%	1.00	10.0%	0.10
Fiscal Flexibility (A): Own-Source Revenues	1	1	16.7%			
Fiscal Flexibility (B): Spending	1	1	16.7%			
Fiscal Flexibility (C): Extent of Borrowing	1	1	16.6%			
<b>Factor 3: Financial Position &amp; Performance</b>						
Interest Payments/Operating Revenue (%)	4.9	6	25.0%	5.50	10.0%	0.55
Cash Financing Surplus(Req)/Total Revenue (%)	-4.4	9	25.0%			
Gross Operating Balance/Operating Revenue (%)	15.0	6	25.0%			
Net Working Capital/Total Expenditures	87.4	1	25.0%			
<b>Factor 4: Debt Profile</b>						
Net Direct and Indirect Debt/Operating Revenue	113.8	9	50.0%	7.75	10.0%	0.78
Short-Term Direct Debt/Direct Debt (%)	8.7	1	25.0%			
Net Debt/Operating Revenue Trend	5.9	12	25.0%			
<b>Factor 5: Governance &amp; Management</b>						
Fiscal Management	1	1	40.0%	1.00	10.0%	0.10
Investment & Debt Management	1	1	20.0%			
Transparency & Disclosure (A)	1	1	15.0%			
Transparency & Disclosure (B)	1	1	15.0%			
Institutional Capacity	1	1	10.0%			
<b>Factor 6: Economic Fundamentals</b>						
Regional or Local GDP pc PPP - estimated (\$US)	37,683	1	100.0%	1.00	10.0%	0.10
<b>Estimated BCA</b>						<b>2</b>



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