S&P Global Ratings

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Summary:

City of Edmonton

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City of Edmonton

Issuer Credit Rating	AA/Stable/A-1+

Key Rating Factors

Credit context and assumptions	Base-case expectations
Prudent financial management practices will support the City of Edmonton's creditworthiness as economic activity recovers. • Despite its large public sector and high income levels, the city's exposure to the volatile energy sector will add to the negative impact from COVID-19 amid low oil prices and ongoing pipeline capacity constraints. • We expect management will continue to make prudent fiscal decisions, allowing it to preserve healthy operating results and remain on track with its large capital plan. • We believe the city's relationship with the Province of Alberta will remain well-balanced and generally supportive.	Effective cost-cutting measures will help offset the budgetary shortfall as a result of COVID-19. • We believe restrictions in place to address the pandemic will have a notable but temporary impact on operating results, largely restricted to the current fiscal year. • The city will proceed with the bulk of its capital program as planned to stimulate the economy, keeping after-capital balances in a deficit. • We expect the debt burden to grow with the capital plan but remain manageable, while liquidity levels continue to be healthy.

Outlook

The stable outlook reflects our opinion that, in the next two years, the revenue and expenditure impacts stemming from the pandemic-related restrictions will be largely temporary in nature and Edmonton will maintain overall sound financial results and secure the pay-as-you-go funding required under its large capital plan. This will allow the city to avoid additional debt borrowing beyond current expectations or excessive drawdowns of reserves. We also expect that the economy will return to moderate growth in the outlook horizon.

Downside scenario

Weaker-than-expected economic activity could impair Edmonton's property tax and user-fee revenues. If this, or an unexpected major spending decision, were to happen while the city is undertaking its large capital spending plan, Edmonton's after-capital deficits and budget flexibility could weaken further. We could lower the rating as a result.

Upside scenario

We could raise the rating in the next two years if Edmonton's economy became less reliant on the energy sector; and robust economic growth supported strong revenue generation, allowing the city to improve its medium-term capital funding profile and fiscal position. Under this scenario, we would expect after-capital deficits to decline consistently below 5% of operating revenues, and the tax-supported debt burden to drop below 120% of operating revenues.

Rationale

We expect the slowdown in economic activity brought about by the COVID-19 pandemic and associated restrictions will create a challenging operating environment for Edmonton in the next two years. Exposure to the energy sector and the currently low oil prices add further uncertainty to the city's recovery path, compared with that of peers with more diversified local economies. Nevertheless, we believe that Edmonton's prudent financial management and cost-containment efforts will help to mitigate the direct fiscal impacts stemming from the pandemic and maintain healthy liquidity levels. The city's large capital plan will continue to drive after-capital deficits and increased borrowings.

Slower economic growth is ahead; financial management remains strong.

Despite what we view as a temporary shock, we believe Edmonton continues to demonstrate characteristics of a strong economy, with an estimated GDP per capita of more than US$41,000 and above the national average. The Edmonton region is the design and fabrication center for most of the equipment used in the oil sands and other oilfield development. This results in high income levels but represents substantial economic concentration. As the provincial capital, Edmonton's economy has historically been anchored by a large public sector, which partially insulates the labor force from economic cycles.

In our opinion, the management team is experienced and qualified to effectively enact appropriate fiscal policies, as well as respond to external risks, most recently to the COVID-19 pandemic. The city has a robust set of financial policies and a well-documented financial plan. In addition, it provides transparent disclosure of pertinent information. Management prepares detailed four-year operating and capital budgets, coinciding with council terms, as well as a 10-year capital investment plan. Management of debt and liquidity is prudent, and the business plan details formal risk-management strategies and policies. We expect these practices to continue over the next two years.

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

Cost-cutting measures will help stabilize operating results amid adverse economic conditions.

To counterbalance the revenue impact of the pandemic, Edmonton is implementing expense-reduction measures to limit the budget shortfall. These include vacancy management, temporary layoffs, and project adjustments, offset somewhat by additional COVID-19 costs, such as enhanced cleaning procedures. Despite a temporary decline in the operating results in 2020, we expect balances will recover and remain healthy, on average, at more than 15% of operating revenues from 2018-2022. Similar to other Canadian municipalities, Edmonton's budgetary flexibility is neutral to our assessment of it budgetary performance, given the city's proven ability to support additional spending while maintaining a manageable fiscal environment.

The city's large capital program will maintain pressure on its after-capital balances, which we forecast will remain in a deficit and average 5.8% of total revenues in the five-year period. We expect Edmonton will proceed with most of the projects to stimulate the economy, spending more than C$3.8 billion through 2022.

With construction of the Valley Line Southeast LRT (stage one) progressing to completion in 2021, and the construction of the Valley Line West LRT (stage two) planned to start the same year, the city expects to issue about C$2.1 billion of total debt from 2020-2022. As a result, we expect that Edmonton's tax-supported debt will rise to about C$4.7 billion in 2022, or 145% of operating revenues. We expect interest expense to remain below 5% of operating revenues in 2019-2021. Our measure of tax-supported debt includes C$587 million debt issued by Edmonton for EPCOR Utilities Inc. (EPCOR). The city's contingent liabilities are low. We do not consider the debt EPCOR issues in its own name as a contingent liability, because we believe the likelihood of the city providing the utility with extraordinary support in a stress scenario is low.

Edmonton continues to benefit from exceptional internal liquidity support and strong access to external liquidity for refinancing needs, given its proven ability to issue into various markets, including that for public debt, and the presence of a secondary market for Canadian municipal debt instruments. Edmonton can also draw up to C$100 million in promissory notes and access the Alberta Capital Finance Authority for term debt financing. We estimate that the city's free cash will total more than C$1.7 billion in the next 12 months, sufficient to cover about 2.9x estimated debt service for the period.

Key Statistics

Table 1

City of Edmonton -- Selected Indicators

	-- Fiscal year ended Dec. 31--					
(Mil. C$)	**2017**	**2018**	**2019**	**2020bc**	**2021bc**	**2022bc**
Operating revenues	2,920	2,921	3,060	2,864	3,146	3,251
Operating expenditures	2,381	2,476	2,545	2,454	2,633	2,746
Operating balance	539	445	514	410	513	506
Operating balance (% of operating revenues)	18.5	15.2	16.8	14.3	16.3	15.5
Capital revenues	470	738	603	515	501	602
Capital expenditures	1,138	1,290	1,259	1,363	1,269	1,186
Balance after capital accounts	(129)	(107)	(142)	(438)	(255)	(78)
Balance after capital accounts (% of total revenues)	(3.8)	(2.9)	(3.9)	(13.0)	(7.0)	(2.0)
Debt repaid	440	461	335	402	431	440
Gross borrowings	586	595	452	657	756	711

Table 1

City of Edmonton -- Selected Indicators (cont.)

	-- Fiscal year ended Dec. 31--					
(Mil. C$)	**2017**	**2018**	**2019**	**2020bc**	**2021bc**	**2022bc**
Balance after borrowings	17	27	(25)	(184)	70	193
Direct debt (outstanding at year-end)	3,534	3,624	3,810	4,122	4,447	4,718
Direct debt (% of operating revenues)	121.0	124.1	124.5	143.9	141.4	145.1
Tax-supported debt (outstanding at year-end)	3,534	3,624	3,810	4,122	4,447	4,718
Tax-supported debt (% of consolidated operating revenues)	121.0	124.1	124.5	143.9	141.4	145.1
Interest (% of operating revenues)	5.0	4.5	4.6	4.5	4.3	4.7
Local GDP per capita (single units)	71,331	72,105	70,704	65,557	66,938	68,090
National GDP per capita (single units)	58,591	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 Edmonton -- Ratings Score Snapshot

Key rating factors	**Scores**
Institutional framework	2
Economy	2
Financial management	1
Budgetary performance	3
Liquidity	1
Debt burden	4
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, April 24, 2020. 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: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- 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

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