Report to Corporate Services Committee

To: Chair and Members
Corporate Services Committee

From: Anna Lisa Barbon, CPA, CGA, Deputy City Manager, Finance Supports

Subject: City of London's Credit Rating

Date: October 7, 2024

Recommendation

That, on the recommendation of the Deputy City Manager, Finance Supports, the City of London's Credit Rating Report, providing a summary of Moody's Investors Service Credit Opinion of the City of London, **BE RECEIVED** for information.

Executive Summary

The City of London has achieved the Aaa ('triple A') credit rating with a stable outlook as part of Moody's Investors Service (Moody's) latest Credit Opinion. Issued on September 12, 2024, this marks the 48th consecutive year of such a rating and represents the highest credit rating issued by Moody's.

Linkage to the Corporate Strategic Plan

Council's 2023-2027 Strategic Plan for the City of London identifies 'Londoners experience good stewardship, exceptional and valued service' as an outcome of the "Well Run City" strategic area of focus. Maintaining London's finances in a transparent, sustainable and well-planned manner by adhering to robust financial policies and practices has helped the City maintain positive operating results, stable debt levels, and strong liquidity, reflected in the credit rating assigned by Moody's.

Analysis

1.0 Background Information

Moody's Ratings publishes credit ratings and provides assessment services on a wide range of debt obligations, programs and facilities, and the entities that issue such obligations in markets worldwide, including various corporate, financial institution and governmental obligations, and structured finance securities. Typically, Moody's reviews the credit worthiness of the City of London annually and then assigns the City a credit rating.

The rating process involved a review of the City's 2023 Financial Statements, 2023 Financial Information Return, 2024 Annual Repayment Limit, 2024-2027 Multi-Year Budget and recent relevant reports to Council (e.g. budget monitoring reports and debenture issuance reports). Moody's also utilizes independent research from a variety of sources such as Statistics Canada, comparisons with other municipalities, and news from local media. Along with reviewing and analyzing documents, Moody's arranges a meeting with the City including members of Civic Administration and the Mayor or Deputy Mayor.

The Credit Opinion for the City of London, published September 12, 2024, is attached as **Appendix A** to this report. Consistent with prior years, the City has maintained its Aaa credit rating with a stable outlook. The City has held the Aaa rating since 1977, making 2024 the 48th consecutive year of the Aaa rating and reaffirming that the City's debt has the highest rating possible. The Aaa rating is integral in securing buyers for the City's debentures. Moody's stable outlook "reflects the long track record of solid operating outcomes, which are built on the City's prudent management and long-term planning approach and strong protection to bondholders stemming from a relatively low debt and interest burden as well as sizeable level of reserves."

2.0 Discussion and Considerations

The Moody's Credit Opinion summarizes the City's credit strengths and challenges. The credit strengths of the City support the rating outlook of Aaa while the challenges are factors that could impact the rating in the future.

The City's credit strengths include:

- High levels of cash and investments providing strong liquidity;
- Low debt levels supported by conservative debt management practices;
- Mature, supportive, institutional framework governing municipalities in Ontario; and,
- Track record of generating positive fiscal outcomes highlights robustness of fiscal planning.

Moody's comments regarding the City's track record of generating positive fiscal outcomes are as follows:

*"…*the City of London displays strong governance and management practices, such as the application of multi-year budgets, which helps to promote stable operations. London's history of posting positive operating results, application of strict controls on debt issuance, and conservative debt and investment policies which limit their exposure to market related risks and help ensure relatively smooth debt servicing costs all act as evidence of the city's strong management and governance.*"*

The comments provided by Moody's in their review of the City of London's credit rating further supports the strategy prioritized by Council to ensure Londoners experience good stewardship, exceptional and valued service by ensuring London's finances are maintained in a transparent, sustainable and well planned manner. The application of multi-year budgeting signifies that the City is looking beyond a short-term horizon when planning its finances. The City's Multi-Year Budget provides alignment of longer-term goals with longer-term funding plans, improved accountability and transparency over spending changes. Taking a long-term view with respect to financial matters has led to fiscally responsible decisions, as reflected in the City's credit rating. According to Moody's, "the multi-year budget approach provides sufficient flexibility for the City to adjust the fiscal plan in each year if necessary". Specifically with respect to the adopted 2024-2027 Multi-Year Budget, Moody's acknowledged the future pressures of additional debt requirements by stating: "While debt is expected to increase over the next 3-4 years due to an increase in growth related capital projects, we do not see this as a change in the City's strong debt management policies."

The City's credit challenges outlined by Moody's include the potential for "near-term fiscal pressures stemming from cost escalation and provincial changes."

Consistent with previous years, Moody's notes that a sustained loss of fiscal discipline leading to a material increase in debt or a substantial reduction in accessible financial reserves could place downward pressure on the City's credit rating. A credit rating downgrade or change in outlook to negative by Moody's may cause investors to lose confidence in the City's financial management practices and/or the corresponding quality of the City's debt, potentially affecting the City's ability to raise future financing. This would also increase interest rates at which the City issues debt, which would increase debt servicing costs for the City.

Moody's introduced an explicit reporting of issuers' Environmental, Social and Governance (ESG) Credit Impact Scores (CIS) in 2022. It is important to note that this ESG score is not an evaluation of the City's performance or activities as it relates to ESG but rather a reflection of how ESG factors within the City of London impact credit risk and therefore the credit rating of the City. The CIS is based on a scale from one to five:

CIS – 1; representing positive impact
CIS – 2; representing neutral to low impact

CIS – 3; representing moderately negative impact
CIS – 4; representing highly negative impact
CIS – 5; representing very highly negative impact

The City’s overall ESG CIS is CIS – 2; neutral to low impact. The environmental profile received a score of two; the social profile received a score of two; and the government profile received a score of one, which “captures London's very strong institutional and governance framework” according to Moody’s. This overall rating is consistent with prior year.

Lastly, while Moody’s updated its rating methodology for regional and local governments in May 2024, it should be noted that the City of London has maintained its Aaa rating under this new methodology.

3.0 Financial Impact/Considerations

The Moody’s Credit Opinion does not have a direct financial impact but affects the rates at which the City is able to issue debt, which in turn affects the City’s debt servicing costs. The Aaa rating allows the City to issue debt at favourable rates as debentures rated Aaa are perceived to have less risk of default.

Conclusion

The City’s achievement of Moody’s Aaa credit rating for 48 consecutive years is a testament to the success of the City’s prudent, conservative approach to fiscal planning and related policies. Maintaining this top credit rating through a period with continued impacts from high inflation and a challenging Multi-Year Budget process is a testament to the flexibility and adaptability of the City’s financial policies and processes.

Prepared by: **Folakemi Ajibola, CTP, ACMA, CGMA Manager, Financial Modelling, Forecasting and Systems Control (Treasury)**

Submitted by: **Kyle Murray, CPA, CA, Director, Financial Planning and Business Support**

Recommended by: **Anna Lisa Barbon, CPA, CGA, Deputy City Manager, Finance Supports**

Appendix “A”

MOODY'S RATINGS

Sub-Sovereign

CREDIT OPINION
12 September 2024

Update

Send Your Feedback

RATINGS

London, City of

Domicile	London, Ontario, Canada
Long Term Rating	Aaa
Type	Senior Unsecured - Dom Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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City of London (Canada)

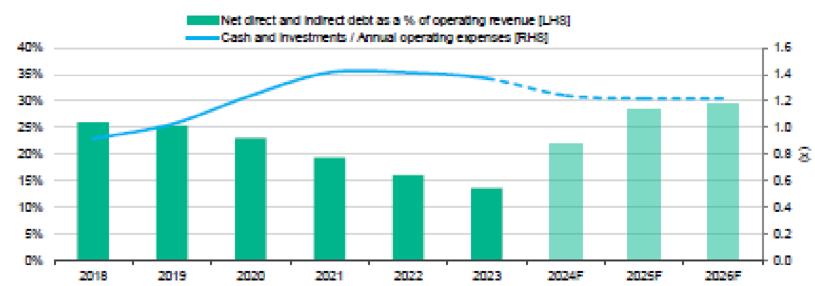
Update following rating affirmation

Summary

The credit profile of the City of London (Aaa stable) reflects the long track record of solid operating outcomes, which are built on the city's prudent management and long-term planning approach. The credit profile also reflects the strong protection to bondholders stemming from relatively low debt and interest burdens. The city also holds sizeable levels of reserves which protect against unforeseen pressures. While debt is expected to increase across the next 3-4 years due to an increase in growth related capital projects, we do not see this as a change in the city's strong debt management policies.

Exhibit 1

London's debt burden will rise but remain in line with historical levels recorded by the city while reserves will continue to provide ample coverage of operating expenses



Sources: City of London financial statements and Moody's Ratings

Credit strengths

» High levels of cash and investments provide strong liquidity

» Low debt levels supported by conservative debt management practices

» Mature, supportive, institutional framework governing municipalities in Ontario

» Track record of generating positive fiscal outcomes highlights robustness of fiscal planning

Credit challenges

» Near-term fiscal pressures stemming from cost escalation and provincial changes

Rating outlook

The outlook for London's Aaa debt rating is stable, reflecting our expectation that the city's fiscal management will continue to ensure that operations remain well maintained, liquidity remains strong and debt will continue to remain within our forecasts across the next three years.

Factors that could lead to a downgrade

Downward pressure could arise if the city were to experience a sustained loss of fiscal discipline leading to a material increase in debt or substantial reduction in accessible financial reserves.

Key indicators

Exhibit 2
London, City of

(Year Ending 12/31)	2020	2021	2022	2023	2024F	2025F
Net Direct and Indirect Debt/Operating Revenue (%)	23.1	19.4	16.1	13.7	21.8	28.3
Primary Operating Balance/Operating Revenue (%)	24.6	25.2	24.5	22.2	22.1	22.0
Cash Financing Surplus (Requirement)/Total Revenue (%)	16.9	20.3	9.1	7.5	7.2	7.7
Interest Payments/Operating Revenue (%)	0.7	0.5	0.4	0.4	0.6	0.8
Debt Service/Total Revenue (%)	4.7	4.3	3.4	3.0	3.6	3.6
Capital Spending/Total Expenditures (%)	20.3	19.6	22.3	25.8	24.8	23.9

Sources: City of London financial statements and Moody's Ratings

Detailed credit considerations

On 11 September we affirmed the aaa baseline credit assessment (BCA) and Aaa senior unsecured debt ratings of the City of London and maintained the stable outlook.

The City of London's Aaa rating combines (1) a BCA of aaa, and (2) a high likelihood of extraordinary support coming from the Province of Ontario (Aa3 positive) to prevent a default by London.

Baseline credit assessment

High levels of cash and investments provide strong liquidity

London's credit profile is supported by a strong liquidity position which provides a significant measure of safety for bondholders. London's liquidity ratio, measured as the ratio of cash and cash equivalents as a % of operating revenue ratio, is among the strongest at 34.6% in 2023 relative to the Canadian municipal peer median of 25.0%. The city's cash and investments levels remained strong in 2023, providing 9.0x coverage of net direct and indirect debt and 1.4x coverage of annual operating expenses. To achieve these levels, the city has continued to follow prudent fiscal management and liquidity policies across multiple changes in the municipal council, which we expect to continue into the future.

London's investment policies ensure that the city minimizes credit risk and maintains liquidity of its investment portfolio. The city's policies outline various limits placed on investment decisions, such as limiting the concentration of investments in specific sectors or issuers, limiting investments to only highly rated securities and ensuring a variety of maturities. The presence and adherence to these policies offers reassurance that the city's investment management policies provide security to liquidity, which along with the level of liquidity, is a strong credit positive.

Low debt levels supported by conservative debt management practices

London's net direct and indirect debt expressed as a percentage of operating revenues measured 13.7% in 2023. While Canadian municipalities can only issue debt for capital reasons, which therefore helps limit indebtedness, London's debt burden is low even compared to domestic peers. Even though Canadian municipalities' revenue structure and high level of operating expense tend to not favour funding capital needs from operations, London has successfully oriented its budget process to minimize debt needs while still implementing necessary capital projects. The city's 2024-2033 capital plan totals CAD5.7 billion across tax-supported and rate-supported projects.

The low debt burden is propelled by the conservative debt policies that the city employs such as a self-imposed "debt cap" which limits the amount of debt that can be issued for capital projects as well as the move to a greater reliance on pay-as-you-go financing. Debt issuance is also reduced through the use of multiple policies overseeing the use of excess funds at year end: the city applies all year-end debt service savings, 50% of unallocated assessment growth as well as 50% of any operating surplus that it generates towards financing needs that would have otherwise be funded from authorized debt issuance. The city has also eliminated debt for lifecycle maintenance of capital, which limits debt issuance to new and/or growth related needs.

The low debt burden also translates into a relatively low interest expense. In 2023, interest expense consumed only 0.4% of operating revenues. Given the efforts to minimize debt issuance, the city's debt service costs as a percentage of revenue are expected to remain low in the intermediate term even as interest expenses rise.

Mature, supportive institutional framework governing municipalities in Ontario
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. Municipalities are, however, subject to the powers and responsibilities imposed upon them by their respective provinces. 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.

London'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 London to manage pressures as they arise.

Track record of generating positive fiscal outcomes highlights robustness of fiscal planning
Similar to other highly rated Ontario municipalities, the City of London displays strong governance and management practices, such as the application of multi-year budgets, which helps to promote stable operations. London's history of posting positive operating results, application of strict controls on debt issuance, and conservative debt and investment policies which limit their exposure to market related risks and help ensure relatively smooth debt servicing costs all act as evidence of the city's strong management and governance.

The city manages its plans using a four-year budget that is prepared during the first year of a new council and extends into the first year of the following council period. Through this process, annual departmental expenditures for the four years are determined in the initial budget year, and in theory only expenditures that are supported through additional assessment growth can be passed outside of the initial budget. City Council can still raise property taxes above the four-year planned approved rates as part of the annual budget review process. Despite the multi-year approach, this budget model provides sufficient flexibility for London to adjust the fiscal plan in each year if necessary.

Near-term fiscal pressures stemming from cost escalation and provincial changes
Despite the track record of sound positive operating outcomes, the city faces ongoing challenges which arise from a variety of sources. These include increased costs for most goods and services, high energy costs and elevated interest rates that represent a significant shift than those recorded over the previous decade. While the city benefits from multi-year collective agreements with the majority of its labour force, we anticipate that as contracts expire, unions will seek higher than previous wage adjustments to reflect the higher cost of living.

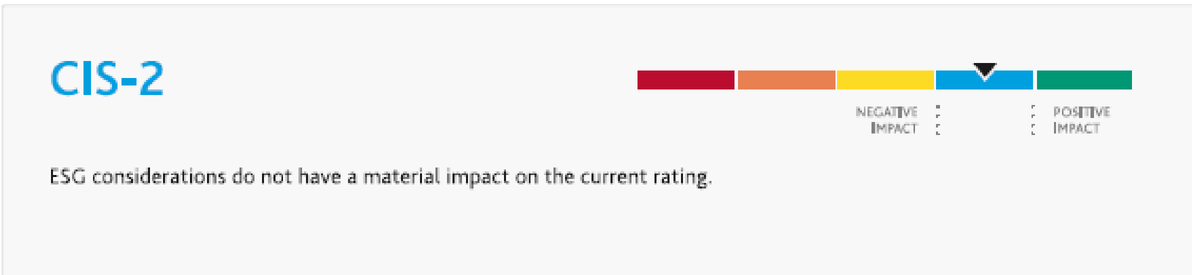
The federal and provincial government's push to develop more housing quicker than the city had previously planned will likely also lead to an accelerated plan for infrastructure projects in undeveloped lands. While this change would disrupt the current long-term plans of the city, London's holdings of development charges are sufficient to continue with plans in the near term and alleviate any immediate credit pressure, while other options facing the city include raising property taxes or deferring capital projects.

Additional provincial changes include the assignment of 'strong mayor' powers to London along with many other large municipalities in Ontario. Under the 'strong mayor' system, the mayor can assume the responsibility of preparing the budget, appoint chairs to committees and boards and have a veto on certain motions brought to council. The latter however is subject to the veto being to support motions in-line with provincial priorities. Although granting these powers does not meaningfully change the governance of the city, the linkage of the veto to provincial priorities increases the risk of indirect intervention by the province in municipal affairs.

ESG considerations

London, City of's ESG credit impact score is CIS-2

Exhibit 3
ESG credit impact score



Source: Moody's Ratings

London's **CIS-2** ESG Credit Impact Score reflects the low exposure to environmental and social risk considerations, any presence of which is further mitigated by the very strong governance and policy effectiveness of the city.

Exhibit 4
ESG issuer profile scores

Source: Moody's Ratings

Environmental

The E issuer profile score (IPS) is **E-2**, reflecting that neither the city's infrastructure nor economic base are subject to material risks stemming from environmental concerns. The city's relatively small geographic footprint and high regulations on water management and waste further minimizes any exposure to environmental risks.

Social

The **S-2** IPS captures the city's role in providing key public services such as public safety (police, fire and paramedic) and environmental (water and waste collection), but demand for these services do not face risks from social considerations given the stable population levels and predictable demographic trends which allows for long-term forecasting of such service requirements. London has a high level of education and overall strong levels of public health and safety.

Governance

The positive **G-1** IPS captures London's very strong institutional and governance framework. The city utilizes prudent financing planning, including the establishment of a 4-year budget plan, and makes use of forward looking assumptions which provides the city with the ability to identify potential pressures and allows for sufficient time to adjust plans accordingly to mitigate any credit implications. The city provides transparent, timely financial reports and adheres to strict policies on debt and investment management.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Extraordinary support considerations

Moody's assigns a high likelihood of extraordinary support from the Province of Ontario (Aa3 positive), reflecting Moody's assessment of the incentive provided to the provincial government of minimizing the risk of potential disruptions to capital markets if London, or any other Ontario municipality, were to default.

Rating methodology and scorecard factors

In the case of London, the assigned BCA of aaa is the same as the BCA scorecard-indicated outcome. For details of our rating approach, please refer to the methodology Regional and Local Governments, 28 May 2024.

Exhibit 5
London, City of
Regional & Local Governments

Baseline Credit Assessment – Scorecard	Score	Value	Sub-factor Weighting	Sub-factor Score	Factor Weighting	Total
Factor 1: Economy					**25%**	**1.03**
Regional Income [1]	2.90	57069.04	15%	0.43		
Economic Growth	9.00	baa	5%	0.45		
Economic Diversification	3.00	aa	5%	0.15		
Factor 2: Institutional Framework and Governance					**30%**	**0.30**
Institutional Framework	1.00	aaa	15%	0.15		
Governance	1.00	aaa	15%	0.15		
Factor 3: Financial Performance					**20%**	**0.60**
Operating Margin [2]	2.70	22.19%	10%	0.27		
Liquidity Ratio [3]	0.50	34.64%	5%	0.03		
Ease of Access to Funding	6.00	a	5%	0.30		
Factor 4: Leverage					**25%**	**0.30**
Debt Burden [4]	1.19	13.72%	15%	0.18		
Interest Burden [5]	1.26	0.38%	10%	0.13		
Preliminary BCA Scorecard-Indicated Outcome (SIO)						**(2.23) aa1**
Idiosyncratic Notching						**1.0**
Preliminary BCA SIO After Idiosyncratic Notching						**(1.23) aaa**
Sovereign Rating Threshold						**Aaa**
Operating Environment Notching						**1.5**
BCA Scorecard-Indicated Outcome						**(1.00) aaa**
Assigned BCA						**aaa**

[1] Regional GDP per capita in terms of purchasing power parity (PPP) terms, in international dollars
[2] Primary Operating Balance / Operating Revenue
[3] Cash and Cash Equivalents / Operating Revenue
[4] Net Direct and Indirect Debt / Operating Revenue
[5] Interest Payments / Operating Revenue
Source: Moody's Ratings; Fiscal 2023.

Ratings

Exhibit 6

Category	Moody's Rating
LONDON, CITY OF	
Outlook	Stable
Baseline Credit Assessment	aaa
Senior Unsecured -Dom Curr	Aaa

Source: Moody's Ratings

REPORT NUMBER 1416255

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454