MOODY'S
INVESTORS SERVICE

CREDIT ANALYSIS

London, City of

London, Ontario, Canada

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This Credit Analysis provides an in-depth discussion of credit rating(s) for London, City of and should be read in conjunction with Moody's most recent Credit Opinion and rating information available on Moody's website.

Ratings

London, City of

Category	Moody's Rating
Outlook	Stable
Sample Entry	Aaa

Summary Rating Rationale

The Aaa debt rating assigned to the City of London (Canada) reflects a low debt profile supported by high reserve levels and a continued management approach classified by prudent, conservative fiscal planning. The city has generated consolidated surpluses since 2005, and in 2011, the consolidated surplus measured C$118 million, equivalent to 11.3% of total revenues. While London's net direct and indirect debt as a percentage of total revenues increased to 38.4% in 2011 from 30.2% in 2010, the city's debt burden remains low and is expected to stay relatively stable over the medium term. London's cash and investments, which represented 110% of net direct and indirect debt at December 31, 2011, provide considerable liquidity and a measure of safety for debenture holders, supporting the Aaa rating.

National Peer Comparisons

The City of London is rated at the high end of Canadian municipalities, whose ratings remain in a narrow range of Aaa-Aa2. When compared with other Canadian municipalities, London exhibits a lower debt burden, while the city's liquidity, as measured by the level of net cash and investments relative to debt and revenue, is considered healthy and in line with national rating peers, strengthening London's credit profile.

Rating Outlook

The rating outlook is stable.

What Could Change the Rating – Down

Given the history of prudent expenditure and debt management, relative stability of the local economy and high fund balances, it is unlikely that conditions could deteriorate by a large enough margin, in the near term, to cause a downgrade. Nonetheless, a sustained loss of discipline, leading to a significant increase in debt, would apply downward pressure on the rating.

Key Rating Considerations

Financial Position and Performance

Surpluses Recorded Since 2005

As a large, relatively self-contained urban center surrounded by smaller rural communities, London is able to profit from a stable economic and demographic environment. City managers operate with five-year operating plans that take advantage of stable and predictable growth estimates, which aid in achieving consistent financial results. The city's targets are, by nature, conservative, helping to identify and address future challenges before they arise. We view the city's rigorous medium-term planning as a key determinant of the Aaa rating.

The city's revenue base is stable and predictable, providing dependable cash flows to meet operating requirements. In 2011, own-source property tax revenue accounted for approximately 52% of operating revenues, while government grants and user rates for water and sewer accounted for approximately 19% and 23% of operating revenues respectively. Property tax receipts and utility charges are relatively uncorrelated with the economic cycle, generating stable revenue flows in periods of economic expansion, as well as in slowdowns.

London's expense base is also predictable, with public safety, transportation services, social and family services and environmental services collectively accounting for over 80% of operating expenses. Expenses have generally grown more slowly than revenues, helping to ensure the posting of generally positive results. From 2005 to 2011, London has generated consolidated surplus that averaged 11.6% of total revenues, allowing the city to build reserves and fund capital expenditures on a pay-as-you-go basis, thereby reducing the city's reliance on borrowing.

Healthy Results Continued in 2011; Pressures Manageable

In 2011, reflecting a 4.5% increase in expenditures and a 5.7% decline in total revenues, London registered a lower surplus of C$118 million, compared to C$221 million a year ago. However, the decline in total revenues was due to a fall in government grants for capital projects, which were unusually high for 2010 as a result of significant funds received through various infrastructure stimulus programs. In 2011, London's revenues from taxation and user fees continued to rise, and the overall surplus position, equivalent to 11.3% of total revenues, remains healthy and roughly in line with the outcome from recent years.

For London's 2012 budget, a 0% increase in property tax levy was maintained for a second consecutive year. Budgetary pressures were addressed through increases in utility rates and efficiency measures resulting from position management and service level changes, although these efficiencies are becoming harder to achieve and a third year of 0% tax increases will be more difficult to maintain. Nevertheless, London has been able to secure labour contracts with several of its unions until 2014, which will help the city manage its expenses. Additionally, the staggered transfer of costs through to 2020 associated with the Ontario Works program to the provincial government is expected to ease some pressure from expense growth and further increase the financial flexibility of the city. While the continual decline in water consumption as a result of conservation will create pressures on rates revenues, the city also has the option of changing its fee structure to address changing consumption habits.

Debt Profile

Prudent Debt Management

London's debt management practices have traditionally been prudent and conservative, which supports its high credit rating. The city's debt burden, measured by the ratio of net debt as a percentage of total revenues, declined in recent years to 30.2% in 2010, from 54.8% in 2004. This progressive reduction in the city's debt burden reflects tighter controls on debt issuance through a self-imposed "debt cap" limiting the amount of debt issued for capital projects, as well as increased reliance on pay-as-you-go financing.

Recent Increase in Debt Manageable

To fund capital projects, London issued debt of C$132 million in 2011, which increased the city's debt outstanding to C$401 million (38.4% of total revenues) at December 31, 2011, from C$334 million (30.2% of total revenues) at December 31, 2010. However, net debt as percentage of total revenues continues to compare favorably to other municipalities. Furthermore, reflecting the current low interest rate environment, in 2011 interest payments consumed only 1.2% of the city's operating revenues, a level that is easily manageable.

The city's latest five-year tax and rates supported capital plans (2012-2016) calls for total capital expenditures of C$992 million, of which C$249 million, or 25.1% of total required funding, will be debt financed. London is expecting to issue about C$70 million of debt in 2012, and if the current capital plan comes to fruition, we anticipate that the city's debt burden would stay near the current level and remains consistent with the current rating.

Strong Liquidity Position Supports Credit Profile

Excluding sinking funds, cash and investments held by the city were equal to 110% of net direct and indirect debt in 2011. While cash and investments in the form of reserves are usually earmarked for specific purposes, London's significant holdings of cash and investments provide a measure of safety for bondholders, supporting the Aaa rating. The high level of liquidity allows the city to be selective and remain out of the market when conditions are considered to be unfavourable. Historically, the city has borrowed from its reserves to provide internal financing for capital projects, and reserve levels are expected to decline in the medium-term to fund the city's latest capital plans. However, London's liquidity is expected to remain more than adequate over the forecast horizon.

Governance and Management Factors

Similar to other highly rated municipalities in Ontario, the City of London displays strong governance and management characteristics. In addition to multi-year planning for operating and capital budgeting and a recent history of meeting fiscal targets and applying strict controls on debt issuance, management adheres to conservative debt and investment management policies, which limits the city's exposure to market-related risks and helps to ensure relatively smooth debt servicing costs. These fiscal management measures are also supported by comprehensive, transparent and timely financial reporting that is typical of governments in advanced industrial countries. In September 2011, London updated its Strategic Plan outlining key priorities identified for 2011-14, and the city is also currently seeking inputs from residents to formulate a new long-term Master Plan, which was last published in 1991.

Economic Fundamentals

The City of London has a relatively diverse economic base and typically is able to provide sufficient employment for its population of approximately 366,000. Located mid-way between Toronto and

Detroit, it is situated along the principal transportation connections through southern Ontario, giving it access to important North American markets, including the US Northeastern and Midwestern regions. Population trends in the city increase at relatively slow, steady rates - population has increased by an average of 0.7% annually from 2007 to 2011 – allowing the city to develop stable growth forecasts for service requirements.

In 2011, London's service sector accounted for about 80% of total employment, with important concentrations in finance, education and health care services. The economy benefits from a well-educated labour force, and several large institutions are also located in the city, including Western University, three teaching hospitals and two large medical research institutes. The city and surrounding region also have a significant manufacturing sector, which has been in decline in recent years, similar to recent trends seen across Ontario and Canada.

As a result of the recent recession, London's unemployment rate increased to 9.9% in 2009, and while labour market conditions are gradually improving, the unemployment rate in the first quarter of 2012 remains elevated at approximately 8.3%. Recognizing that the economic structure of southern Ontario is in transformation, with a decreased presence of automobile manufacturing and a Canadian dollar fluctuating near parity with the American dollar, the city is very active in the pursuit of attracting companies with leading edge technology that can benefit from the well-educated labour force and research centers to continue to bolster the high-value added sectors of the economy.

Operating Environment

The national operating environment in which London 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 low 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.

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.

Application of Joint-Default Analysis

The application of Moody's joint-default analysis methodology to regional and local governments (RLGs) requires two key inputs: a baseline credit assessment (BCA), which is a measure of the RLG's standalone credit strength, and an assessment of the likelihood that the higher-tier government would act to prevent a default by the RLG. In the case of London, Moody's assigns a BCA of aaa, which already places the city in the Aaa rating category before any consideration of the likelihood that the

Province of Ontario (Aa2, stable outlook) would act to prevent a default by London. To complete the analysis, Moody's assigns a very high likelihood of extraordinary support from the provincial government, reflecting Moody's assessment of the risk to Ontario's reputation as a regulator of municipalities and the province's aversion to the potential impact on capital markets if London, or any municipal government, were to default.

Rating History

London, City of

Date	Rating
December 1977	Aaa

Annual Statistics

London, City of					
Debt Statement (C$000, as at 12/31)	**2007**	**2008**	**2009**	**2010**	**2011**
Debt Issued for:					
General Municipality	388,041	358,239	319,587	330,471	397,851
Other Municipalities	5,424	4,408	3,328	3,029	2,716
Net Direct and Indirect Debt	**393,465**	**362,647**	**322,915**	**333,500**	**400,567**
Debt Trends (as at 12/31)					
Net Direct and Indirect Debt (C$000)	393,465	362,647	322,915	333,500	400,567
As % Total Revenues	43.6	36.5	32.7	30.2	38.4
As % Operating Revenues	48.5	41.7	36.5	35.3	43.0
As % of Taxable Assessments	1.5	1.4	1.1	1.1	1.3
As % of Net Direct and Indirect Debt					
General Municipality Purposes	98.6	98.8	99.0	99.1	99.3
Other Municipalities	1.4	1.2	1.0	0.9	0.7
Debt per Capita (C$)	1,106	1,011	891	913	1,094
Net Debt Issuances (C$000)	47,718	6,099	0	45,393	132,077

[1] Net direct and indirect debt as a percent of full market value of assessment.

Economic Trends (Year Ending 12/31)	2007	2008	2009	2010	2011
Population	355,596	358,838	362,235	365,200	366,150
Taxable Assessment - Full Value (C$ Millions) [1]	26,074	26,590	28,445	30,085	31,969
% Change	2.0	2.0	7.0	5.8	6.3
Current Tax Collection Rate (%)	94.2	94.8	93.4	94.0	94.3
Value Building Permits (C$ Millions)	722.2	799.0	553.0	711.9	1,008.7
Unemployment Rate (%)	6.1	7.1	9.9	8.6	9.0
Unemployment Rate, Province (%)	6.4	6.5	9.0	8.7	7.8

[1] Series impacted by periodic reassessments; not all data points are directly comparable.

Revenues and Expenses (C$000, year ending 12/31)	2007	2008 [1]	2009	2010	2011
Revenues:					
Taxation	421,319	442,927	464,260	476,790	482,669
User fees and Services [2]	126,968	193,789	195,813	215,788	216,216
Provincial Grants	160,352	164,949	160,146	181,640	173,468
Federal Grants		1,690	4,253	11,428	1,418
Investment Income		15,021	6,566	6,790	6,572
Other Revenues	193,210	52,101	53,632	51,968	50,843
Provincial and Federal Capital Grants		53,287	28,332	100,368	47,438
Gain/loss on Sale of Land/Capital Assets		-4,709	-6,173	-3,311	-6,082
Development Charges		26,659	19,877	29,111	32,823
Developer Contributions of Tangible Capital Assets		48,785	60,292	35,435	37,558
Total Revenues	**901,848**	**994,499**	**986,998**	**1,106,007**	**1,042,923**
Expenses					
General Administration	34,609	72,245	74,720	80,791	81,436
Protection to Persons and Property	144,768	146,156	153,507	169,432	171,998
Transportation Services	92,313	134,418	129,905	147,473	146,118
Environmental Services	75,191	137,332	140,513	129,747	140,304
Social and Family Services	187,622	189,493	198,955	199,616	189,782
Social Housing	37,728	41,768	44,031	51,914	45,584
Interest Payments [3]	12,180				
Principal Payments	31,751				
Health Services	31,049	19,765	20,017	20,695	21,141
Recreation and Culture	55,425	68,174	68,176	69,501	80,031
Planning and Development	16,865	21,855	16,964	16,329	48,915
Other Expenses	127,367		8,638		
Total Expenses	**846,868**	**831,206**	**855,426**	**885,498**	**925,309**
Surplus (deficit)	**54,980**	**163,293**	**131,572**	**220,509**	**117,614**
Cash Financing Surplus/(Requirement)	**98,287**	**90,277**	**-7,482**	**-14,298**	**37,659**
Cash Financing Surplus/(Requirement) net of CAPEX	274,291	270,208	214,132	291,592	228,939
Capital Expenditures	176,004	170,861	221,614	305,890	191,280
Debt Repayment	31,751	40,660	47,222	39,323	87,053
Amortization [3]		108,475	112,721	119,154	127,239
Interest [3]		15,581	14,179	13,356	11,637

[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.

[2] Prior to 2008, includes only water, sewer and transit charges.

[3] Subsumed in other expense categories beginning in 2008.

London, City of

Financial Trends (Year Ending 12/31)	2007	2008 [1]	2009	2010	2011
Operating Revenues [2]	810,689	870,477	884,670	944,404	931,186
Operating Expenses [3]	719,501	722,731	734,067	766,344	798,070
Gross Operating Balance [4]	**122,939**	**147,746**	**150,603**	**178,060**	**133,116**
% Change in Total Revenues	**6.2**	**10.3**	**(0.8)**	**12.1**	**(5.7)**
As % Operating Revenues					
Taxation	52.0	50.9	52.5	50.5	51.8
Provincial Grants	19.8	18.9	18.1	19.2	18.6
User Fees and Services [5]	15.7	22.3	22.1	22.8	23.2
Interest Expense	1.9	1.8	1.6	1.4	1.2
Reserves and Reserve Funds	33.0	49.3	51.8	49.1	52.8
Surplus/(Deficit)	6.8	18.8	14.9	23.3	12.6
Gross Operating Balance	15.2	17.0	17.0	18.9	14.3
As % Total Revenues					
Surplus/(Deficit)	6.1	16.4	13.3	19.9	11.3
Financing Surplus/(Requirement)	10.9	9.1	(0.8)	(1.3)	3.6
Financing Surplus/(Requirement) excl. CAPEX	30.4	27.2	21.7	26.4	22.0
Debt Service [6]	5.3	5.7	6.2	4.8	9.5
% Change in Total Expenses	**11.2**	**(1.8)**	**2.9**	**3.5**	**4.5**
As % Operating Expenses					
Protection to Persons and Property	20.1	20.2	20.9	22.1	21.6
Social and Family Services	26.1	26.2	27.1	26.0	23.8
Debt Services [6]	6.6	7.8	8.4	6.9	12.4

[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.

[2] Starting in 2008, total revenues less development charges, government capital grants, gains/losses on sale of land/capital assets and developer contributions of tangible capital assets is used as a proxy for operating revenues.

[3] Starting in 2008, total expenses less amortization is used as a proxy for operating expenses. Prior to 2008, includes principal payments.

[4] Revenues less expenses, excluding development charges, government capital grants, gains/losses on sale of land/capital assets, developer contributions of tangible capital assets and amortization. Prior to 2008, gross operating balance is calculated as operating revenues less operating expenses excluding principal payments.

[5] Prior to 2008, includes only water, sewer and transit charges.

[6] Principal and interest.

London, City of

Consolidated Balance Sheet (C$000, As At 12/31)	2007	2008 [1]	2009	2010	2011
Cash and Investments [2]	349,447	407,243	353,196	326,718	440,564
As a % of Net Direct and Indirect Debt [3]	88.8	112.3	109.4	98.0	110.0
Receivables	72,277	59,571	93,123	110,081	85,813
Payables	102,220	99,959	107,294	127,495	118,912
Fund Balances					
Reserves	57,040	65,200	91,396	88,356	102,843
Reserve Funds	204,965	220,624	214,551	245,028	257,169
Deferred Revenues (Including Development Charges)	117,344	142,938	152,331	130,073	131,587

[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.

[2] Includes long-term investments.

[3] Cash and investments less sinking funds as a % of net direct and indirect debt.

Moody's Related Research

Analysis:

» Ontario, Province of, May 2012 (141981)

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» Canadian Provinces Consolidating Finances in 2012, March 2012 (140455)

» Canadian Municipalities: Remaining Strong in Turbulent Times, February 2012 (139798)

Statistical Handbook:

» Non-U.S. Regional and Local Governments, June 2012 (141944)

Rating Methodologies:

» Regional and Local Governments Outside the US, May 2008 (107844)

» The Application of Joint-Default Analysis to Regional and Local Governments, December 2008 (99025)

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